Katz, Bennett

From: Hipschen, June
Sent: Friday, January 08, 1999 7:56 PM
To: Barnes, Ray; Cobb, Anne; Eitingon, Daniel; Fry, Derek; Goggin, Dennis M.; Katz, Bennett; Partridge, James; Pascarella, Carl; Van Der Velde, Hans; Williamson, Malcolm
Cc: Burry, Sue; De Wouters, Geraldine; Everoski, Dee; Giesker, Theresa; Ponzo, Terri; Powell, Alicia; Shields, Susie; Socash, Madeleine; Spiller, Kaye; Vincent, Joanna; Sho, Hairei
Subject: MEC Advance Materials - January 1999
Importance: High
Sensitivity: Confidential

The attached advance materials for discussion at the upcoming MEC meeting are being sent to you on behalf of Stephen Schapp of Emerging Products, Una Somerville of Current Products & Services and Mark Tremont of International Finance.

If you have any difficulty in opening these files, please contact June Hipschen via e-mail or by calling OCW 2159.

Thank you.

Infrastructure Migration Strategy and Business Case

MEC IMS Exec Summ 1-99.doc

Inter-Regional Interchange Reimbursement Fees

MEC Interchange Exec Sum199.doc

Customer Authentication Service (Informational only - <u>NO</u> presentation or discussion planned)

MEC Authentication Exc Sum 199.doc

P-0543

GOVERNMENT DEPOSITION EXHIBIT 901

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VISA INTERNATIONAL

MANAGEMENT EXECUTIVE COMMITTEE

San Francisco, California
18-19 January 1999

EXECUTIVE SUMMARY

Infrastructure Migration Strategy and Business Case

The Infrastructure Migration Strategy is a set of milestones to enhance the global payment service infrastructure and extend its value for Members in the next decade. The overall strategy was reviewed with the International Board at its meeting in Buenos Aires. With the support of the MEC, management proposes to request International Board endorsement of the global Infrastructure Migration Strategy and approval of the first phase of implementation. To support this proposal, a financial analysis of the migration costs and benefits has been prepared and will be shared with the MEC and the Board.

The Infrastructure Migration Strategy is based upon three key categories of business drivers:

- Baseline: Enhancements to the payment service to reduce fraud, achieve operating efficiencies, and expand usage.
- Protect: Member issuance of multifunction relationship cards that leverage the baseline infrastructure and help protect banks' payment franchise from non-bank competitors.
- Extend: Introduction of value-added services that drive increased card usage.

Several actions are proposed to respond to these business drivers. Migration to chip will help combat skimmed counterfeit, achieve operating efficiencies from off-line transactions, and securely expand usage to additional points of convenience. In addition, the strategy proposes point-of-transaction support at chip devices for Issuer optional use of PIN, with signature continuing as the default method of cardholder verification. The ability to verify the customer's identity is important for fraud control, particularly as the mix of payment transactions consists of fewer face-to-face transactions. Operational and quality enhancements are also included in conjunction with chip and PIN infrastructure changes. These enhancements comprise reduced clearing windows, improved data quality, and transaction matching, which will help to better manage available balances and risk, improve customer service, and reduce exception items.

The costs and benefits of these actions have been assessed in a business case analysis of the migration strategy. The business case includes assessment of worldwide aggregate costs and benefits over a ten-year period, from the year

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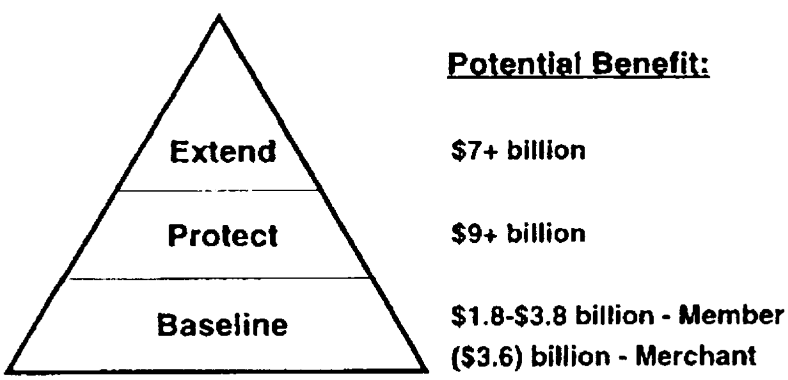
2000 through 2009, assuming the infrastructure enhancements are completed within a five-year period, from 2000 to 2005. Costs and benefits are included for major participants in the payment service—Issuers, Acquirers, and merchants—for their Visa and MasterCard programs. The financial analysis focuses primarily on the Baseline enhancements, and estimates the potential benefits of the Protect and Extend categories. Conservative assumptions have been made throughout the analysis to ensure that net benefits are not overstated.

Assumptions supporting the business case incorporate available quantitative data, the input of content experts among Region and Central staff, and the input of Members who have implemented similar infrastructure changes. It also is being reviewed by the CFOs in each Region and at Central.

The analysis suggests that Visa Members may benefit from the baseline enhancements alone, with significant additional potential in the Protect and Extend categories. However, merchants incur a net cost for baseline changes.



These results support several conclusions:

- The baseline actions represent a reasonable investment to improve the payment service and to establish a foundation for protecting and extending Members' payment franchise. The benefits of Protect and Extend could dwarf the net investment in Baseline changes.
- An imbalance in net benefits between Members and merchants will need to be offset to encourage merchants to establish the necessary chip acceptance infrastructure.
- It is prudent to initiate the Infrastructure Migration Strategy for those actions which require the longest lead time for implementation. The goal is to impact the next buy decision for systems, terminals and cards so that

multiple replacement costs are avoided and benefits are derived more quickly.

It is therefore proposed that the following actions be submitted to the International Board for consideration at the February meeting:

- Endorsement of the overall Infrastructure Migration Strategy, with an end vision defined as follows:
  - ◊ All Visa cards are chip cards and Visa point-of-transaction devices can read them.
  - ◊ All Visa cards and devices are EMV and interoperable.
  - ◊ All Visa point-of-transaction chip devices support PINs.
  - ◊ Visa account numbers can be up to 19 digits.
  - ◊ Clearing times for electronic transactions are three days.
  - ◊ Quality of authorization data is improved.
  - ◊ Transactions are matched.

- Approval of the Foundation Building phase of the migration strategy, encompassing the following milestones:
  - ◊ All existing Visa chip cards and devices to be fully EMV compliant by 1 January 2003.
  - ◊ All new terminals and electronic cash registers to be chip and PIN "capable"—at a minimum containing a chip/PIN pad port—beginning no later than 1 January 2001.
  - ◊ All Visa chip accepting devices ~~to~~ have a PIN pad by 1 January 2003 liability shift
  - ◊ All new ATMs to have chip and magnetic stripe readers beginning no later than 1 January 2003.

It is further proposed that a Transitional Infrastructure Fee be established effective in the year 2000 to encourage placement of EMV compliant chip terminals. Details of this proposal are provided in the MEC materials entitled Inter-Regional International Interchange Reimbursement Fees. Consideration should also be given to an International Board resolution requesting the six Regional Boards to adopt programs and incentives to encourage chip/PIN terminal installation.

The next steps following Board approval are to:

- Develop rollout plans for key markets whose business case is most driven by the need for infrastructure change.
- Communicate the migration strategy to Members and merchants.
- Encourage card, terminal, and system vendors to support the migration.

Stephen Schapp
Una Somerville

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Attachment
Business Case Assumptions

This attachment describes the high-level business case assumptions for the Baseline, Protect and Extend categories of business drivers. The Baseline category includes payment service changes to avoid fraud, achieve operational efficiencies, and expand usage.

Fraud Avoidance

Skimmed counterfeit reported by key Members in Asia, Canada, the United Kingdom, and the United States has more than doubled in less than a year. Although absolute global skimming losses are relatively low, the global average growth in total counterfeit was 44% from 1996 to 1997, and is estimated to be approximately 35% from 1997 to 1998 due to the impact of recent countermeasures. Skimmed counterfeit appears to be an increasingly significant element of the total counterfeit. Given the fact that no potential additional countermeasures have been identified, it is difficult to project how rapidly skimming will grow in future years. Therefore, the business case analysis assesses the business impact of a low skimming growth rate and a high skimming growth rate.

The business case assumes that skimming continues to increase significantly with magnetic stripe technology. Member risk management groups agree that magnetic stripe technology is inadequate for combating skimmed counterfeit, and that chip with a secure authentication method is the most viable solution. Business case scenarios estimate that the threat of skimmed counterfeit can be reduced by 70%-90% through the implementation of chip cards that provide a secure card authentication method, achieved when a critical mass of cards and terminals is in place worldwide.

Apart from skimmed counterfeit, the fraudulent use of lost and stolen cards is the largest grouping of fraud losses in most markets, and is estimated to be over US$1 billion in 1998 for Visa and MasterCard programs. As the mix of payment transactions includes fewer face-to-face transactions, the ability to verify the customer's identity becomes even more important. Therefore, the Infrastructure Migration Strategy proposes point-of-transaction support for Issuer optional use of PIN, with signature continuing as the default method of cardholder verification. The migration strategy includes milestones to add PIN pad capability at the time of conversion to chip capability. Although biometric forms of cardholder verification are not precluded, PINs are today the most proven, reliable and common way of identifying customers by a number of industries.

The business case assumes that 90% of lost and stolen fraud can be avoided for transactions using chip and PIN to verify a cardholder's identity. In order to achieve these savings, the migration strategy specifies that all chip devices can support a PIN pad by the year 2001. Reflecting the fact that PIN is currently the predominant cardholder verification method for domestic debit programs, the business case assumes that ultimately 80% of Visa debit programs will migrate to PIN at the time they convert to chip, taking advantage of greater security and lower terminal conversion costs. The business case assumes that 25% of Visa credit programs will migrate to PIN at the time of chip conversion, since some key markets already are considering a transition to PIN for credit.

Operating Efficiencies

As Members capture a greater share of Personal Consumption Expenditure from cash and check, they will continue to tap into markets in which on-line transactions are not cost effective. The business case estimates the incremental cost and benefit of using chip cards to complete transactions off-line, including using chip to verify PINs off-line. The off-line PIN verification process is a secure way to verify the cardholder at the point-of-transaction without requiring an on-line message to the Issuer.

The business case assumes that 40% of chip transactions will be completed off-line, blending markets in which almost no transactions will be authorized off-line with those in which 80% will be authorized off-line. It is assumed that the percentage of off-line transactions will grow to 60% worldwide by the year 2009 as Members gain a greater share of cash and check transactions and average transaction values decline. For off-line chip transactions, it is assumed that Issuers and Acquirers will achieve savings in processing costs for incremental off-line transactions, and that merchants will achieve savings in telecommunications costs as well as labor savings resulting from improved throughput at checkout.

Expanded Usage

Today, identifying a customer on the Internet is carried out by software that is customized to contain user authentication information. Competitive industries, concluding that this is limiting to their users, are exploring chip cards as a way to allow portability and security in accessing the Internet from a variety of devices. It is envisioned that the banking industry also would benefit from customers using the portability and security of chip to increase Internet purchases. The business case assumes that these features will result in a 10% increase in Internet purchases over and above industry predicted increases.

Additional Baseline Opportunities

There is opportunity for business value in making additional infrastructure changes at the time of making the Baseline changes described above. Other payment service changes can be made at lower incremental cost when they are done along with chip and PIN infrastructure changes. These include reduced clearing windows, improved data quality, and transaction matching.

Reducing clearing windows allow Issuers to better manage available balances. When a merchant delays settlement or does not complete the sale, the Issuer must decide when to release the authorization hold placed on the available balance. Releasing the hold too early opens the Issuer to the risk of fraud or credit loss. Holding the funds too long results in unnecessary declines and customer dissatisfaction. Fast settlement is particularly critical for debit transactions where the available balance is usually lower than for credit products.

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In addition, there is opportunity to improve the accuracy of data currently provided. Accurate authorization data facilitates early fraud detection and prevention, and increases approval rates for customers. Issuers use parameters based on authorization data to determine if an on-line authorization is required, if further credit should be extended, or if the cardholder spending pattern is unusual. If the authorization data is inaccurate, Issuers may decline good transactions or miss fraud warnings that would have generated declines or referrals. Accurate settlement data is key in reducing costs associated with exception item processing. Merchants who supply inaccurate or confusing data in the settlement record see more copy request and chargebacks from cardholders who challenge transactions they do not recognize.

Authorization and settlement data need to be not only accurate but also consistent for the same transaction. The ability to match the authorization to the settlement record increases the Issuer's ability to manage the cardholder's available balance and can reduce the number of exception items. Authorization holds can be released more quickly when the Issuer is confident that the matching settlement has cleared. In addition, invalid chargebacks and representments can be systematically edited and rejected before they reach the intended recipient.

The business case estimates the net benefit of these infrastructure changes to be US$0.5 billion NPV. These benefits have not been included in the financial model.

Protecting the Payment Franchise

The ability to protect the payment service franchise is a business value that can be layered onto the foundation of Baseline changes. Foremost among challenges facing the banking industry is the growing threat from emerging competitors. Increasingly, telecommunications operators, software companies, retailers, mass transit operators, and others are looking at payment services as a natural extension of their core businesses. If the threat of large-scale disintermediation materializes, a portion of Members' card net income—approximately US$300 billion NPV over the next ten years —will be at risk.

Considering all major industries, analysts predict that the banking industry will represent barely 10% of chip cards by the year 2003. This means that in sheer numbers of chip cards other industries are laying the basis for becoming customers' base multiple function card. One disintermediation scenario features a major player in a key competitive industry establishing a strong base of their own multiple function cards. A major telecommunications company, for example, could be the first to establish a critical mass of multiple function cards that have broad consumer appeal. Banks could be relegated to providing wholesale payment services on a telephone company branded card with significantly lower income.

Recent history provides examples of industries that have made transitions or risked losing the value they built. One of the most powerful examples of disintermediation occurred in the computer industry, where value moved away from proprietary mainframes and minicomputer systems to workstations and PCs. From 1984 to 1994, IBM and DEC lost US$55 billion in market value, while Microsoft, Intel, EDS, and Novell were gaining US$80 billion.[1] In th~ ; :yment services industry, a loss of just 3% of card net income for the years 2000-2009 amounts to US$9 billion net present value.

The Infrastructure Migration Strategy proposes a set of changes that Members can leverage to:

- Compete with other industry multiple function cards
- Maintain bank cards as the preferred card
- Continue the bank payment service as the anchor service on multiple function cards
- Provide access to services over the Internet
- Extend services that meet customer demand for convenience

Extending services

Another area of value that Members can layer onto Baseline infrastructure changes is additional opportunity to provide convenience and utility to their customers. In offering a rich set of functions, including the ability to access services from a wide variety of usage locations, bank cards will retain the "top-of-wallet" status that payment cards enjoy today as the most important item in customers' wallets. Banks will add functions to their cards that are adapted to the needs of a particular customer relationship.

The business case analysis assumes that multiple function cards will account for 80% of card volume by the year 2009. Since value-added services will be unique to individual Members, the business case does not estimate their incremental value, assuming that the cost of providing these services will at least be covered by their incremental revenue. It assumes that there will be a 10% increase in payment service transactions generated by value-added services such as loyalty programs, travel and entertainment applications, or transit applications. This results in a potential benefit of US$7 billion (NPV).

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[1] Slywotzky, Adrian J., "Value Migration," 1996

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VISA INTERNATIONAL

MANAGEMENT EXECUTIVE COMMITTEE MEETING

San Francisco, California
18-19 January 1999

EXECUTIVE SUMMARY

Inter-Regional International Interchange Reimbursement Fees

The inter-Regional International Interchange Rate structure was modified in 1994 to introduce an electronic rate of 1.0 percent, and increase the standard rate from 1.0 percent to 1.44 percent These rates apply to transactions which flow between Visa Regions. Intra-Regional and domestic interchange rates apply to all other transactions, however, many markets default to the international fee structure. While new rates have been established for new products, such as Commercial Cards and Visa Infinite, the basic international rate structure and rate values have not changed since 1994. Over the past five years, changes in factors influencing these rates have resulted in rate adjustments in many local markets; yet the inter-Regional rates have not been adjusted. It is proposed that the following recommendation to bring the inter-Regional rates into alignment with current market conditions be presented to the International Board in February. Concurrently, a new fee structure to advance the Infrastructure Migration Strategy is proposed as described below.

These adjustments will more accurately reflect current payment service costs, reduce the subsidization of MasterCard at the point of sale, and provide a longer term interchange structure incorporating new technologies.

Recommendation

- Gradually increase the standard and electronic inter-Regional interchange rates[1] to reflect current market factors as follows:

	Electronic	Standard
CURRENT	1.00%	1.44%
2000	1.10%	1.60%
2001*	1.25%	1.70%
2002*	1.40%	1.80%

*Decisions on actual rates beyond 2000 would not be taken at this time. This information is provided for direction setting only and would not be shared with the Board in advance materials. Future rates would be reviewed and adjusted annually based upon prevailing market conditions.

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[1] See Attachment A for current rate definitions and qualification criteria.

- Introduce a new incentive structure in 2000 to support the Infrastructure Migration Strategy.

  This incentive structure would establish an offset or credit against the inter-Regional Interchange Rates defined above to benefit Acquirers which initiate the migration to chip terminals for POS transactions or SET for Internet transactions. In subsequent years, this incentive would be extended to transactions which include enhanced transaction data to address the acceptance quality aspects of the Infrastructure Migration Strategy.

  These "Transitional Infrastructure Fees" would apply to those transactions initiated at EMV chip devices or with merchants using SET merchant certificates when the Issuer is employing "old" technology - magnetic stripe or lack of cardholder SET certificates. Once Issuers have made the transition, the Interchange Rates would normalize at the Standard or Electronic rate level. This approach assures that payment service players are equally motivated to migration. Merchants migrate to chip and SET certificates to achieve the best effective rate. Issuers are encouraged to migrate to achieve the best effective rate. By introducing these new incentive levels concurrent with the overall rate increase, it is believed the impact to Acquirers in key markets will be mitigated while providing overall support for our strategic objectives. The proposed rate structure is described in Attachment C.

Rationale

- Financial Justification

  In a recent analysis using the same methodology that has been employed through the years in Headquarters and the Regions, the inter-Regional interchange rate was recalculated and found to be significantly higher than the previous calculated rate. The new rate calculation derived in August 1998 was 1.98 percent. The major increases are related to costs associated with attracting, maintaining, and servicing customers, credit write-offs, and fraud losses, which for inter-Regional transactions have increased to 40-50 basis points on sales.

- Business Drivers

  Given the wide gap between the current rate and the newly calculated rate, Visa Issuers are being under-compensated for inter-Regional transactions. In addition, the MasterCard inter-Regional interchange rates are significantly higher than for Visa (see Attachment B). Currently, the gap between Visa and MasterCard is roughly 20 basis points on sales in lost Issuer revenue for inter-Regional Visa transactions. With an announced MasterCard rate hike (effective April '99), that differential will increase to over 30 basis points on non-electronic transactions. In some cases, Issuers have identified this factor as an influence in brand decisions despite inter-Regional volume being relatively small.

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It should also be noted that MasterCard rates to Acquirers for international transactions are even higher than the rates that are passed on to MasterCard Issuers as interchange income. It is believed that this differential is used by MasterCard to fund initiatives.

- Timing

The proposal is to increase the electronic rate to 1.10 percent and the standard rate to 1.60 percent in 2000, for a blended effective rate of 1.30 percent, based on the present mix. This places Visa in a favorable market situation with both Acquirers and Issuers. The goal is to adjust rates upwards each subsequent year; however, to provide market flexibility, it is recommended that action on these rates not be taken in advance.

Given Y2K constraints for both Members and Visa, the first opportunity to adjust rates will be with the first system release of 2000. By providing more than 12 months advance notice, Members, particularly Acquirers, will have ample opportunity to plan for the rate increase. Issuer brand decisions now at risk may be saved by providing immediate advance notice of the planned increase next year. It is recognized that any rate increase may be negatively perceived by Acquirers and Merchants, thus a pragmatic, multi-year adjustment is proposed to achieve multiple goals for appropriately compensating Issuers without abrupt or significant pricing increases to Acquirers and Merchants.

- Synchronization with Infrastructure Migration Strategy

In evaluating the Visa inter-Regional interchange structure, future requirements have been evaluated as part of a multi-year approach. With the completion of the Infrastructure Migration Strategy business case analysis, it became clear that the interchange structure must be considered as a mechanism to provide an incentive for infrastructure migration and to equalize the cost benefit equation between acquiring and issuing. With the need to raise current interchange rates coinciding with the launch of the Infrastructure Migration Strategy, it is appropriate to consider a proposed structure for chip and Internet transactions concurrently.

The inter-Regional interchange reimbursement rates are not necessarily effective by themselves in motivating market change because international volumes are relatively small. However, the inter-Regional rates often serve as a model for domestic rates. To the extent that the inter-Regional rate structure is implemented domestically, it will have a positive and lasting impact. In addition, there is significant market influence in announcing a fee structure tied to the infrastructure migration. It demonstrates a firm commitment to the marketplace, and historically has proven to be more influential in motivating action than mandates.

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Following discussion at the MEC meeting, this proposal will be brought to the International Board concurrently with the Infrastructure Migration Strategy in February.

Una Somerville
Mark Tremont

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Attachment A

Current Service Definitions

Electronic

- Card and Cardholder present
- Magnetic stripe is read and the entire unaltered contents of the magnetic stripe are transmitted in the authorization message (for CVV consideration)
- Authorized through VisaNet
- Cleared and settled within five calendar days, excluding Sunday and the transaction date
- Electronic indicator is present

Standard

- Transactions which do not qualify as electronic and are not product-specific (see below)

Product Specific

- Commercial Card
- Visa Infinite - same rate as Commercial Card
- Visa Electron - processed under the "electronic rate" definition
- Interlink

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Attachment B

Point of Sale Inter-Regional Interchange Rates

	Visa	MasterCard(i)
Electronic	1.00%*	1.16%
Standard	1.44%	1.65%
Blended	1.18%	1.35%

*This includes Electron and Visa Smart Debit/Credit transactions

(i)Present effective rates based on an average inter-Regional transaction size of U.S. $121.00.

Note: MasterCard rates are scheduled to increase in April 1999 as follows:

	Acquirer Charged	Issuer Receives
Electronic	1.37%	1.16%
Standard	2.18%	1.77%

It is believed that MasterCard International keeps 20-40 basis points from each transaction to fund initiatives.

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Attachment C

Proposed Inter-Regional Interchange Reimbursement Fee Structure

The proposed rate structure consists of:

1. Increasing the two existing inter-Regional rates (i.e., standard and electronic)
2. Defining two additional incentive rates for electronic commerce and chip
3. Implementing a rate modifier applicable to the electronic and chip incentive rates when certain enhanced transaction data quality standards are met.

The following material defines the rates, explains how the rates will motivate desired performance, and presents a hypothetical rate structure.

Rate Definitions

Standard	Applies to traditional non-electronic transactions and e-commerce transactions. Same definition as today.
Electronic	Applies to magnetic-stripe transactions at magnetic-stripe terminals, or chip transactions at EMV chip terminals. This is a new definition of the electronic rate.
SET Transitional Infrastructure Fee Incentive	Applies to SET e-commerce transactions that include SET Merchant certificates, but not cardholder certificates. This is a new incentive rate designed to motivate migration of Merchants to SET. This incentive will automatically be eliminated over time as cardholder certificates become prevalent.
Chip Transitional Infrastructure Fee Incentive	Applies to magnetic-stripe transactions at EMV compliant chip terminals. This is a new rate designed to motivate Acquirers to implement chip terminals. This incentive will also be automatically eliminated over time as chip cards become prevalent.
Enhanced Transaction Data Fee Incentive	The electronic and chip incentive rates can be reduced by an Acquirer that meets certain processing standards.

Motivational Forces

Electronic Commerce: There are two desired outcomes - a migration of Merchants to provide SET Merchant certificates, and issuance of cardholder certificates. The rate proposal motivates both. Because there are very few cardholder certificates currently issued, Acquirers will be motivated to support SET Merchant certificates in order to achieve the SET incentive rate. Once a SET Merchant infrastructure is in place, Issuers will be motivated to provide cardholder certificates to gain the additional interchange offered by the standard rate. Merchants will, however, benefit from the fraud protection provided by the cardholder certificate in the transaction, offsetting the increased cost. The SET incentive rate is a transitional rate. Over time, more and more e-commerce transactions will be completed at the standard rate.

Chip: There are two desired outcomes - the implementation of EMV chip acceptance devices, and the issuance of chip cards. The rate proposal motivates both. Initially, Acquirers will be motivated to implement terminals capable of reading EMV chip cards. All magnetic-stripe transactions at chip terminals, initially almost all electronic transactions, will qualify for the lower chip incentive rate. Once the chip terminal infrastructure is largely in place, Issuers will be motivated to issue chip cards in order to achieve the electronic rate. As with the SET incentive rate, the chip incentive rate can be considered transitional. Over time, a higher percentage of transactions will qualify for the electronic rate.

Acceptance Quality: It is desirable to motivate specific performance by Acquirers to achieve higher acceptance quality. Providing PIN support, delivering improved data quality, and improving transaction clearing times are examples. An Acquirer can achieve a lower interchange rate for transactions that would otherwise qualify for the electronic or chip rates by providing transactions that meet the requirements. (Note: this concept could also apply to Commercial Card transactions with or without enhanced data.)

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Hypothetical Rate Structure

The chart below shows hypothetical rates for the proposed rate structure:

	1999	2000	2001	2002
Standard IRF Rate	**1.44%**	**1.60%**	**1.70%**	**1.80%**
SET Transitional Incentive Fee	n/a	-.16%	-.16%	-.16%
SET Transitional Incentive Effective Rate	n/a	1.44%	1.54%	1.64%
Electronic IRF Rate	**1.00%**	**1.10%**	**1.25%**	**1.40%**
Chip Transitional Incentive Fee	n/a	-.10%	-.10%	-.10%
Chip Transitional Incentive Effective Rate	n/a	1.00%	1.15%	1.30%
Enhanced Transaction Data Incentive (Decrease applied to either electronic or chip rates for specific Acquirer performance)	n/a	n/a	-.10%	-.10%

Example Transactions

The following table shows sample transactions, the rates that would apply today and the rates that would apply with the proposed structure in 2000.

Transaction Description	Processing Environment	Current Rate	New Rate Structure
Electronic commerce	No SET certificate	1.44%	1.60%
Electronic commerce	Merchant certificate only	1.44%	1.44%
Electronic commerce	Merchant and cardholder certificates	1.44%	1.60%
Face to face	Magnetic-stripe terminal, chip card	1.00%	1.10%
Face to face	EMV chip terminal, magnetic- stripe card	1.00%	1.00%
Face to face	Chip terminal, chip card	1.00%	1.10%

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VISA INTERNATIONA

MANAGEMENT EXECUTIVE COMMITTEE MEETING

San Francisco, California
18-19 January 1999

EXECUTIVE SUMMARY

Customer Authentication Service

Visa's electronic commerce strategy has a dual focus – to establish Visa as the preferred payment brand for Internet purchases while working to build a more secure Internet infrastructure for the future. Programs to build a more secure infrastructure were initially directed at securing Visa card purchases through the development and implementation of SET. An essential component of SET includes mutual authentication between the cardholder and merchant.

The Internet has led more and more companies to leverage the low-cost telecommunications and global connectivity for commerce purposes. As an open network, however, the Internet presents business issues which must be addressed for companies to fully leverage the potential benefits of the Internet. These include: 1) the inability to identify the other party for a transaction and 2) the ease with which data can be intercepted and copied. These issues can be resolved through the use of authentication services. The importance of authentication is expected to grow as multifunction chip cards are used to access a wide variety of third-party services, in the Internet as well as the physical world.

As a commerce environment, the Internet creates global opportunities. Because business may be easily conducted country-to-country, Internet authentication services will sought allowing participants to place a high level of trust and confidence on the actual identity authentication. Visa, with its worldwide membership of financial institutions, would be uniquely positioned to developed a branded authentication service.

Through the use of encryption, authentication services provide identity validation, the basis for non-repudiation of data and information exchanged between the parties, and confidentiality/privacy of the transaction. It is important to note that the service focuses on validating the identity of parties involved in Internet commerce transactions – and is not necessarily related to payment or Visa account relationships; but rather, commerce in the broadest sense of the term. Examples of the uses of authentication services are highlighted below:

- A company wants to use the Internet to distribute a request for proposal to multiple companies and receive binding bids from suppliers. Through the use of an authenticated digital signature, a supplier's response becomes the equivalent of a signed, written proposal.

- A government agency wants to use an authentication service to identify individuals submitting requests to qualify for government transfers, such as unemployment benefits or other social welfare benefits.
- A health care organization wants to reduce costs and permit physicians and patients to remotely access medical records. Authentication services provide the means to permit access to such confidential information files.
- An airline wants to offer upgrade awards through acceptance of its loyalty partners chip cards, validating the identity of qualified passengers.

A number of authentication services have been introduced in the market. Some of the providers are banks, however, many non-banks are active as well. Highlighted below are some of these services:

Banks

- Internet Banking Services -- BNL in Italy, NAB in Australia and Scotia Bank in Canada
- Government Service Pilots -- Barclays (Endorse) and NatWest in the U.K.
- Commercial Services -- Zions' Digital Signature Trust, Bank of America's NACHA Pilot, and Global Trust Organization Consortium of eight leading global banks.

Telecommunications Companies/ Postal Authorities

- Telco Web Sites – British Telecom and Deutsche Telekom
- Authenticated eMail/commercial services (Australia, U.K. and U.S.)

Technology Companies

- Certificate Service/Software Providers: Certco, Entrust and VeriSign
- IBM and Equifax Joint Venture

These authentication services involve the use of general purpose digital certificates, representing a new service opportunity for Visa and its Members. As noted above, banks and others are beginning to explore how these services are marketed. It is expected that authentication services will move from specific company needs to more branded services widely offered to individuals and businesses over the next 12 to 18 months. With this short window of opportunity, the timing is opportune for Visa to evaluate offering a new service to assist its Members in meeting the needs for Internet identity authentication for both retail and commercial customer segments.

A preliminary service assessment has been completed and is currently being reviewed with Region Product/Marketing staff. Region staff are being asked to assist in reviewing the concept proposal with key Members. At the same time, work is underway to develop a full service description, a marketing plan, the business case, processing options, and operating principles. These will be reviewed at a future MEC meeting and are targeted for Board consideration in May/June. This is a briefing document for the MEC. No presentation is planned.

Janet Pruitt

Inter Regional
Interchange Fee

Katz, Bennett

From: Somerville, Una
Sent: Friday, January 08, 1999 8:10 PM
To: Williamson, Malcolm
Cc: Tremont, Mark; Eitingon, Daniel; Barnes, Ray; Katz, Bennett; Schapp, Stephen
Subject: Background for MEC Discussion on Interchange Fees

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VISA

Current Products
& Services

MEMORANDUM

TO: Malcolm Williamson

FROM Una Somerville and Mark Tremont

DATE: 8 January 1999

SUBJECT: **Inter-Regional Interchange Rate Increase Proposal**

On the agenda for the January MEC meeting is a recommendation to increase the inter-Regional International Interchange Reimbursement Fee (IRF). The inter-Regional interchange rates are established by the International Board. The inter-Regional rate applies only to those transactions which flow from Region to Region. Many Regions presently have separate interchange rate structures for transactions within a region and/or domestic market. Some Regions, however, default to the inter-Regional rates.

This proposal has been in circulation with Regional CFOs and product executives. The amount and timing of the increase is described in the attached Executive Summary which has been circulated as advance reading for the MEC.

The methodology for establishing inter-Regional International interchange rates was established many years ago and also is used by the Regions in setting their own rates. The rates have not been increased since 1994.

The business reasons for the increase are multiple:

- The Visa Market rate is 30-40% below the Visa calculated rate; this is due to increased cardholder acquisition and servicing costs, increased credit write-offs, and increased fraud write-offs (inter-Regional fraud is about 40-50 basis points of sales), which means the Issuers are not being adequately reimbursed,

- The effective Visa Market rate is significantly below the current comparable effective MasterCard rate, and MasterCard has communicated yet another rate increase for April 1999, making the gap larger. The net impact of this is Visa subsidization of MasterCard at the point of sale, as many Acquirers simply blend the Visa and MasterCard rates to their merchants. In addition, this has begun to affect brand decisions by card Issuers in Regions such as Asia-Pacific.

An immediate rate adjustment to remedy this situation is not feasible. We must provide adequate market notice and during the Y2K preparations it is not appropriate to impact Members or our own systems with this type of change. In addition, since the gap is quite large, any rapid action to dramatically increase rates may have negative impact perceptions and relations with Acquirers and merchants. Thus, a deliberate and phased approach is recommended to gradually bring the rates to proper levels beginning in 2000.

By bringing our international rates into alignment, we will have more flexibility in applying interchange fee adjustments to advance our infrastructure migration to chip and secure internet commerce. A proposed structure has been defined, and we will review this with the MEC at the meeting. Although incentive interchange structures have significant precedent in motivating market action, the topic is controversial. In reviewing the Infrastructure Migration business case work with Stephen Schapp, it is clear that we must incorporate our view on market incentives as part of and concurrently with the proposed IRF rate increase.

There is no consensus of Regional positions on the fundamental issue of increasing inter-Regional rates. Attached is a matrix outlining the financial impact to each Region and their current position. By introducing an incentive structure for deployment of chip devices, we believe some issues surrounding a general rate increase will be mitigated with EU and CEMEA Acquirers. Our recommendation is to move forward with the proposal, discuss the Regional positions at the MEC and then take the proposal forward to the International Board as planned in February.

Let us know if you would like to meet to review this further.

Impact by Region

Inter-Regional Interchange Rate Increase Proposal

	AP	Canada	CEMEA	EU	LAC	USA
Issuer						
New Rate	$98M	$54M	$13M	$111M	$50.3M	$140M
Old Rate	$89M	$49M	$12M	$102M	$46.0M	$128M
Net Increase	$9M	$5M	$1M	$9M	$4.3M	$12M
Acquirer						
New Rate	$43M	$48M	$23M	$117M	$44.8M	$202M
Old Rate	$47M	$44M	$21M	$107M	$40.7M	$184M
Net Increase	$4M	$4M	$2	$10M	$4.1M	$18M
Net - Benefit/(Loss)	$5M	$2M	($1.4M)	($1M)	$.2M	($5M)
Point of View	**In Favor** Recognize that Issuers are under reimbursed and losing Brand decisions due to competition's higher interchange rates. Will be changing Intra-Regional interchange rates to match competition by February 1999.	**In Favor** Supports application of interchange methodology.	**Against** Would cause a net outflow to Members. Feel IRF is an "economic" justification related to domestic issues rather than international. Increase will perpetuate inefficiency of Issuers.	**Against** Feel IRF is an "economic" justification related to domestic issues rather than international. Suggest if fraud is so high that increase should target that specific problem.	**In Favor** In favor, in principle, to ensure interchange methodology is consistently applied.	**In Favor** w/some conditions Increase could have a significant impact on Regional revenue dynamics, however, a pending domestic interchange decision would positively impact that effect. Domestic decision expected Jan. '99.

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VISA INTERNATIONAL

MANAGEMENT EXECUTIVE COMMITTEE MEETING

San Francisco, California
18-19 January 1999

EXECUTIVE SUMMARY

Inter-Regional International Interchange Reimbursement Fees

The inter-Regional International Interchange Rate structure was modified in 1994 to introduce an electronic rate of 1.0 percent, and increase the standard rate from 1.0 percent to 1.44 percent These rates apply to transactions which flow between Visa Regions. Intra-Regional and domestic interchange rates apply to all other transactions, however, many markets default to the international fee structure. While new rates have been established for new products, such as Commercial Cards and Visa Infinite, the basic international rate structure and rate values have not changed since 1994. Over the past five years, changes in factors influencing these rates have resulted in rate adjustments in many local markets; yet the inter-Regional rates have not been adjusted. It is proposed that the following recommendation to bring the inter-Regional rates into alignment with current market conditions be presented to the International Board in February. Concurrently, a new fee structure to advance the Infrastructure Migration Strategy is proposed as described below.

These adjustments will more accurately reflect current payment service costs, reduce the subsidization of MasterCard at the point of sale, and provide a longer term interchange structure incorporating new technologies.

Recommendation

- Gradually increase the standard and electronic inter-Regional interchange rates[1] to reflect current market factors as follows:

	Electronic	Standard
CURRENT	1.00%	1.44%
2000	1.10%	1.60%
2001*	1.25%	1.70%
2002*	1.40%	1.80%

*Decisions on actual rates beyond 2000 would not be taken at this time. This information is provided for direction setting only and would not be shared with the Board in advance materials. Future rates would be reviewed and adjusted annually based upon prevailing market conditions.

[1] See Attachment A for current rate definitions and qualification criteria.

- Introduce a new incentive structure in 2000 to support the Infrastructure Migration Strategy.

  This incentive structure would establish an offset or credit against the inter-Regional Interchange Rates defined above to benefit Acquirers which initiate the migration to chip terminals for POS transactions or SET for Internet transactions. In subsequent years, this incentive would be extended to transactions which include enhanced transaction data to address the acceptance quality aspects of the Infrastructure Migration Strategy.

  These "Transitional Infrastructure Fees" would apply to those transactions initiated at EMV chip devices or with merchants using SET merchant certificates when the Issuer is employing "old" technology - magnetic stripe or lack of cardholder SET certificates. Once Issuers have made the transition, the Interchange Rates would normalize at the Standard or Electronic rate level. This approach assures that payment service players are equally motivated to migration. Merchants migrate to chip and SET certificates to achieve the best effective rate. Issuers are encouraged to migrate to achieve the best effective rate. By introducing these new incentive levels concurrent with the overall rate increase, it is believed the impact to Acquirers in key markets will be mitigated while providing overall support for our strategic objectives. The proposed rate structure is described in Attachment C.

<u>Rationale</u>

- Financial Justification

  In a recent analysis using the same methodology that has been employed through the years in Headquarters and the Regions; the inter-Regional interchange rate was recalculated and found to be significantly higher than the previous calculated rate. The new rate calculation derived in August 1998 was 1.98 percent. The major increases are related to costs associated with attracting, maintaining, and servicing customers, credit write-offs, and fraud losses, which for inter-Regional transactions have increased to 40-50 basis points on sales.

- Business Drivers

  Given the wide gap between the current rate and the newly calculated rate, Visa Issuers are being under-compensated for inter-Regional transactions. In addition, the MasterCard inter-Regional interchange rates are significantly higher than for Visa (see Attachment B). Currently, the gap between Visa and MasterCard is roughly 20 basis points on sales in lost Issuer revenue for inter-Regional Visa transactions. With an announced MasterCard rate hike (effective April '99), that differential will increase to over 30 basis points on non-electronic transactions. In some cases, Issuers have identified this factor as an influence in brand decisions despite inter-Regional volume being relatively small.

It should also be noted that MasterCard rates to Acquirers for international transactions are even higher than the rates that are passed on to MasterCard Issuers as interchange income. It is believed that this differential is used by MasterCard to fund initiatives.

- Timing

The proposal is to increase the electronic rate to 1.10 percent and the standard rate to 1.60 percent in 2000, for a blended effective rate of 1.30 percent, based on the present mix. This places Visa in a favorable market situation with both Acquirers and Issuers. The goal is to adjust rates upwards each subsequent year; however, to provide market flexibility, it is recommended that action on these rates not be taken in advance.

Given Y2K constraints for both Members and Visa, the first opportunity to adjust rates will be with the first system release of 2000. By providing more than 12 months advance notice, Members, particularly Acquirers, will have ample opportunity to plan for the rate increase. Issuer brand decisions now at risk may be saved by providing immediate advance notice of the planned increase next year. It is recognized that any rate increase may be negatively perceived by Acquirers and Merchants, thus a pragmatic, multi-year adjustment is proposed to achieve multiple goals for appropriately compensating Issuers without abrupt or significant pricing increases to Acquirers and Merchants.

- Synchronization with Infrastructure Migration Strategy

In evaluating the Visa inter-Regional interchange structure, future requirements have been evaluated as part of a multi-year approach. With the completion of the Infrastructure Migration Strategy business case analysis, it became clear that the interchange structure must be considered as a mechanism to provide an incentive for infrastructure migration and to equalize the cost benefit equation between acquiring and issuing. With the need to raise current interchange rates coinciding with the launch of the Infrastructure Migration Strategy, it is appropriate to consider a proposed structure for chip and Internet transactions concurrently.

The inter-Regional interchange reimbursement rates are not necessarily effective by themselves in motivating market change because international volumes are relatively small. However, the inter-Regional rates often serve as a model for domestic rates. To the extent that the inter-Regional rate structure is implemented domestically, it will have a positive and lasting impact. In addition, there is significant market influence in announcing a fee structure tied to the infrastructure migration. It demonstrates a firm commitment to the marketplace, and historically has proven to be more influential in motivating action than mandates.

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Following discussion at the MEC meeting, this proposal will be brought to the International Board concurrently with the Infrastructure Migration Strategy in February.

Una Somerville
Mark Tremont

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Attachment A

Current Service Definitions

Electronic

- Card and Cardholder present
- Magnetic stripe is read and the entire unaltered contents of the magnetic stripe are transmitted in the authorization message (for CVV consideration)
- Authorized through VisaNet
- Cleared and settled within five calendar days, excluding Sunday and the transaction date
- Electronic indicator is present

Standard

- Transactions which do not qualify as electronic and are not product-specific (see below)

Product Specific

- Commercial Card
- Visa Infinite - same rate as Commercial Card
- Visa Electron - processed under the "electronic rate" definition
- Interlink

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Attachment B

Point of Sale Inter-Regional Interchange Rates

	Visa	MasterCard(1)
Electronic	1.00%*	1.16%
Standard	1.44%	1.65%
Blended	1.18%	1.35%

*This includes Electron and Visa Smart Debit/Credit transactions

(1)Present effective rates based on an average inter-Regional transaction size of U.S. $121.00.

Note: MasterCard rates are scheduled to increase in April 1999 as follows:

	Acquirer Charged	Issuer Receives
Electronic	1.37%	1.16%
Standard	2.18%	1.77%

It is believed that MasterCard International keeps 20-40 basis points from each transaction to fund initiatives.

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Attachment C

Proposed Inter-Regional Interchange Reimbursement Fee Structure

The proposed rate structure consists of:

1. Increasing the two existing inter-Regional rates (i.e., standard and electronic)
2. Defining two additional incentive rates for electronic commerce and chip
3. Implementing a rate modifier applicable to the electronic and chip incentive rates when certain enhanced transaction data quality standards are met.

The following material defines the rates, explains how the rates will motivate desired performance, and presents a hypothetical rate structure.

Rate Definitions

Standard	Applies to traditional non-electronic transactions and e-commerce transactions. Same definition as today.
Electronic	Applies to magnetic-stripe transactions at magnetic-stripe terminals, or chip transactions at EMV chip terminals. This is a new definition of the electronic rate.
SET Transitional Infrastructure Fee Incentive	Applies to SET e-commerce transactions that include SET Merchant certificates, but not cardholder certificates. This is a new incentive rate designed to motivate migration of Merchants to SET. This incentive will automatically be eliminated over time as cardholder certificates become prevalent.
Chip Transitional Infrastructure Fee Incentive	Applies to magnetic-stripe transactions at EMV compliant chip terminals. This is a new rate designed to motivate Acquirers to implement chip terminals. This incentive will also be automatically eliminated over time as chip cards become prevalent.
Enhanced Transaction Data Fee Incentive	The electronic and chip incentive rates can be reduced by an Acquirer that meets certain processing standards.

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Motivational Forces

Electronic Commerce: There are two desired outcomes - a migration of Merchants to provide SET Merchant certificates, and issuance of cardholder certificates. The rate proposal motivates both. Because there are very few cardholder certificates currently issued, Acquirers will be motivated to support SET Merchant certificates in order to achieve the SET incentive rate. Once a SET Merchant infrastructure is in place, Issuers will be motivated to provide cardholder certificates to gain the additional interchange offered by the standard rate. Merchants will, however, benefit from the fraud protection provided by the cardholder certificate in the transaction, offsetting the increased cost. The SET incentive rate is a transitional rate. Over time, more and more e-commerce transactions will be completed at the standard rate.

Chip: There are two desired outcomes - the implementation of EMV chip acceptance devices, and the issuance of chip cards. The rate proposal motivates both. Initially, Acquirers will be motivated to implement terminals capable of reading EMV chip cards. All magnetic-stripe transactions at chip terminals, initially almost all electronic transactions, will qualify for the lower chip incentive rate. Once the chip terminal infrastructure is largely in place, Issuers will be motivated to issue chip cards in order to achieve the electronic rate. As with the SET incentive rate, the chip incentive rate can be considered transitional. Over time, a higher percentage of transactions will qualify for the electronic rate.

Acceptance Quality: It is desirable to motivate specific performance by Acquirers to achieve higher acceptance quality. Providing PIN support, delivering improved data quality, and improving transaction clearing times are examples. An Acquirer can achieve a lower interchange rate for transactions that would otherwise qualify for the electronic or chip rates by providing transactions that meet the requirements. (Note: this concept could also apply to Commercial Card transactions with or without enhanced data.)

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Hypothetical Rate Structure

The chart below shows hypothetical rates for the proposed rate structure:

	1999	2000	2001	2002
Standard IRF Rate	**1.44%**	**1.60%**	**1.70%**	**1.80%**
SET Transitional Incentive Fee	n/a	-.16%	-.16%	-.16%
SET Transitional Incentive Effective Rate	n/a	1.44%	1.54%	1.64%
Electronic IRF Rate	**1.00%**	**1.10%**	**1.25%**	**1.40%**
Chip Transitional Incentive Fee	n/a	-.10%	-.10%	-.10%
Chip Transitional Incentive Effective Rate	n/a	1.00%	1.15%	1.30%
Enhanced Transaction Data Incentive (Decrease applied to either electronic or chip rates for specific Acquirer performance)	n/a	n/a	-.10%	-.10%

Example Transactions

The following table shows sample transactions, the rates that would apply today and the rates that would apply with the proposed structure in 2000.

Transaction Description	Processing Environment	Current Rate	New Rate Structure
Electronic commerce	No SET certificate	1.44%	1.60%
Electronic commerce	Merchant certificate only	1.44%	1.44%
Electronic commerce	Merchant and cardholder certificates	1.44%	1.60%
Face to face	Magnetic-stripe terminal, chip card	1.00%	1.10%
Face to face	EMV chip terminal, magnetic- stripe card	1.00%	1.00%
Face to face	Chip terminal, chip card	1.00%	1.10%

Budget

Katz, Bennett

From: Dutt, Ron
Sent: Wednesday, January 06, 1999 10:13 AM
To: Anne Cobb; Bennett Katz; Daniel Eitingon; Dennis Goggin; Derek Fry; Hans Van Der Velde; James Partridge; Malcolm Williamson
Cc: Barnes, Ray; Tremont, Mark
Subject: MEC Financial Summary

On behalf of Ray Barnes, attached is a high level financial summary of Visa Worldwide year-to-date results. As agreed at the November MEC meeting in London, the intent is to provide this report as a premail for each MEC meeting.

Financial Summary

VISA

Key Business Indicators
November 1998
($ in millions)

Year-to-Date Better/(Worse) than Plan	HQ	Visa International	Visa Worldwide
Revenue	15.5	18.7	*
Expenses	12.4	23.2	*
Contingency	0.0	0.0	*
Pre-Tax	27.9	41.9	*
Headcount	90	172	*

Full Year Forecast Better/(Worse) than Plan	HQ	Visa International	Visa Worldwide
Revenue	0.0	0.0	0.0
Expenses	(0.9)	(0.9)	(0.9)
Contingency	0.0	0.0	0.0
Pre-Tax	(0.9)	(0.9)	(0.9)
Headcount	(6)	(6)	(6)

* Worldwide consolidation detail not currently available. Information will be included in next report.

01/15/1999

Venture Capital

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VISA INTERNATIONAL
BOARD OF DIRECTORS MEETING

San Francisco, California
22 February 1999

EXECUTIVE SUMMARY

VISA TECHNOLOGY FUND

Background

New technologies are dramatically changing the financial services industry and, more specifically, the payments industry. Consumer definition of convenience is beginning to shift from physical location to remote access availability. New hardware, software and network technologies are evolving quickly and effective deployment of these technologies will determine which financial service companies prevail in the years ahead.

A number of innovative, new financial services companies are capitalizing on emerging technologies to quickly build strong brands, large customer bases, and significant market capitalizations. One example is E*TRADE, the leading provider of online investing services. E*TRADE's volume has grown ten-fold in the last two years – faster than the rate of growth of the Internet itself. By virtue of this growth, E*TRADE now enjoys annual revenues exceeding $300 million and a market capitalization of $5.7 billion. Other emerging financial service providers leveraging technology to realize tremendous growth include companies such as InsWeb, an online insurance provider; E-Loan, an online mortgage originator; and TeleB@nc, a national branchless bank with assets of over $2 billion.

As these examples illustrate, new technologies hold tremendous potential for Visa Members but also pose threats, as they can be readily utilized by non-traditional competitors to encroach on banks' core business. Visa International is committed to tracking technology trends and to taking a

proactive role in influencing them, wherever feasible, to best represent Members' interests.
A key activity toward this end has been Visa International's strategic investment program. Since 1994, Visa International has achieved substantial strategic and financial benefits for Visa Members through a series of equity investments in emerging technology companies. These equity investments protect Member interests in the rapidly evolving technology arena and generate strong financial gains for Visa Members.

To date, Visa has invested $12.6 million in eleven technology companies and has generated investment gains of more than $225 million, of which $95 million is realized and $130 million is unrealized. This represents an annual IRR of 229%. Exhibit I provides an overview of Visa's current strategic investment portfolio. (Note that Visa International has also made "infrastructure investments" in eight companies such as VisaNet do Brasil and Proton World International).

By forming strategic partnerships with key technology companies, Visa has also realized significant strategic gains. For example, through Visa's investment in Yahoo, the Visa brand is prominently displayed on the Yahoo homepage and throughout their network of web sites. In addition, Visa is positioned as Yahoo's preferred and default card throughout Yahoo's shopping sites.

Another example is Visa's investment in VeriSign, which has enabled Visa to have direct influence on the development of electronic commerce infrastructure to ensure that Visa Members are well positioned in the electronic marketplace. Other investments have also yielded significant financial and strategic value for the Visa Membership.

Competitive Environment

Increasingly, Visa competitors are using venture capital investments to improve their positions in the marketplace. American Express has been very aggressive in the corporate venture capital arena and has a larger and more active venture capital program than Visa.

In the last two years alone, American Express has made over 20 investments in technology and service companies that deliver new sources of revenue as well as strategic value to Amex.

American Express has recently expanded its strategic investment program by forming partnerships with two outside venture capital firms and is the primary limited partner for one of these firms (Peter Halmos & Sons).

Corporate Venture Capital Trend

Across many industries, senior executives have recognized that corporate venture capital is critical to their companies' survival in the face of rapid technological change and is an excellent mechanism for enhancing their internal research and development capabilities. This strategy is evidenced by the establishment of dedicated venture capital programs at companies such as Adobe, Allstate, Ameritech, AOL, AT&T, Bausch & Lomb, Cadence, Cambridge Technology, Cendant, CKS, Cisco, Comcast, Comdisco, Compaq, EW Scripps, Ernst & Young, Exxon, First Data, General Electric, Gillette, Hewlett Packard, Hitachi, Humana, IDG Ventures, Intel, Itocha, John Hancock, Johnson & Johnson, Knight-Ridder, Lucent, MCI Worldcom, Microsoft, Mobil Oil, Monsanto, Motorola, Netscape, Newscorp, Nokia, Northern Telecom, Novell, Oracle, Quark, SAP, Sega, Siemens, Softbank, Sun, TCI, Texas Instruments, Toshiba, United Airlines, US West, UPS, Xerox and Yahoo.

Proposal

While Visa Members have to date benefited indirectly from Visa's strategic investment program, management proposes that a vehicle be created that would:

a) enable Visa Members to receive direct financial and strategic benefits by co-investing with Visa in companies that are strategically important to their business, and

b) bring more professional venture capital discipline and controls to Visa's current investment activities.

The Visa Technology Fund would accomplish both of these objectives and would allow Visa Members more direct access to promising and innovative technology companies.

The charter of the Visa Technology Fund would be two-fold. First and foremost, the fund would invest in companies that provide new technologies, products or services that are strategically important to Visa Members. Second, the fund would deliver exceptional financial returns to Visa Members who choose to invest in the fund.

Visa International would act as the fund's general partner. Interested Visa Members would be limited partners. To provide professional fund management, the Visa Technology Fund would partner with a top-tier investment bank or venture capital firm.
The primary focus of the fund managers would be to identify investments in new payment technologies, such as chip cards, electronic payment systems, security / fraud control technologies and electronic commerce technologies. A secondary focus would be placed on new technologies that more broadly benefit the banking industry, such as new delivery mechanisms for financial services.

The Visa Technology Fund would aim to achieve an annual rate of return of not less than 20% (historically Visa has achieved a 229% annual return on its technology portfolio). Fund investments would range from $500,000 to $15 million, with the vast majority of financings ranging between $1 million to $5 million. The fund would operate a balanced portfolio, representing a mix of both early and later stage investments.

Due to Visa Headquarters office proximity to Silicon Valley, the Visa Technology Fund is perfectly positioned to exploit the tremendous technological innovation occurring in this area. Visa Members who are limited partners would have a window on critical new technologies and promising enterprises incubating in Silicon Valley. Roughly 70% of the investments would be made in the Silicon Valley area.

The Visa Technology Fund would be funded by Visa International as well as interested Visa Members. To initiate the fund, Visa International would reinvest $75 million (one-third of its $225 million investment gains to date) from its current portfolio of liquid and non-liquid investments in technology companies. Interested Visa Members could elect to invest from $5 million to $50 million each, depending upon their level of interest.

Written reports regarding market intelligence, fund activities and fund performance would be provided to the Visa International Board and fund partners three times per year. In addition, the fund would hold an annual technology conference and provide a password-protected website for fund investors.

Key Benefits

The proposed Visa Technology Fund would deliver the following benefits:

- Enable Members to directly participate in the strategic and financial benefits of Visa's existing strategic investments.
- Provide Members with improved access to the technologies that affect their payments business.
- Evolve Visa's current investment activities into a more competitive, professional program with more formalized discipline, controls and reporting.
- Leverage Visa's geographic proximity to Silicon Valley to provide Members a window into the high volume of technology innovations.
- Through partnership with a top-tier investment bank/venture capital firm, establish a more formalized process and structure for sourcing, evaluating, negotiating, executing, tracking and exiting investments.
- Enable Members to supplement their own corporate R&D efforts and/or venture capital programs by electing to participate in the Visa Technology Fund.

While all Visa Members have benefited from Visa's strategic investments in the past and will continue to do so in the future, the Visa Technology Fund would enable interested Members to invest additional capital to a) receive a higher, more direct return and b) gain greater insight into technology developments through the fund's market intelligence reports and advisory meetings.

To date, the investment gains that Visa has realized through its technology investments have funded critical Visa projects, strengthened the Visa brand and improved Visa's capital base.

Going forward, future gains will be used to fund this new investment program and reduce the brand fee for Visa Members.

Exhibit II provides additional information regarding Visa's strategic investment program and the proposed Visa Technology Fund.

Exhibit I

Visa International Strategic Investments
($ millions)

Technology Portfolio	Investment Amount	Current Value [1]
• Ariba Technologies	$ 0.75	$ 1.50
• CyberSource, Inc.	$ 1.50	$ 2.50
• Epiphany, Inc.	$ 1.70	$ 1.70
• Extensity, Inc.	$ 1.50	$ 3.00
• Intelidata, Inc.*	$ 0.66	$ 1.86
• Nuance Comm.	$ 0.75	$ 15.00
• Open Market *	$ 1.50	$ 2.00
• Trintech, Inc.	$ 1.50	$ 3.00
• VeriSign, Inc.*	$ 1.37	$ 59.81
• Worlds, Inc.*	$ 1.10	$ 0.22
• Yahoo, Inc.*	$ 0.30	$146.69 [2]
Subtotal	**$12.63**	**$237.28**
Infrastructure Portfolio		
• Ecomm, LLC.	$ 1.15	$ 1.15
• GP Network Corp.	$ 0.19	$ 0.19
• Proton World Int'l.	$13.00	$ 13.00
• Transaction Tech.	$ 0.45	$ 0.45
• Visa Argentina	$ 0.75	$ 7.00
• VisaNet do Brasil	$ 0.62	$ 98.00
• Visa Jordan	$ 0.55	$ 0.55
• Visa Peru	$ 0.38	$ 2.00
Subtotal	**$17.09**	**$122.34**
TOTAL	**$29.72**	**$359.62**

* Investments that have gone public
[1] Includes realized and unrealized gains
[2] Includes $45M in contractual advertising/brand support

Year 2000

From: Eitingon, Daniel
Sent: Wednesday, December 23, 1998 4:02 PM
To: Williamson, Malcolm; Goggin, Dennis M.; Fry, Derek; Barnes, Ray; Katz, Bennett; Pascarella, Carl; Partridge, James; VAN DER VELDE, HANS; COBB, ANNE
Cc: Gregory, Laura; Elliott, Linda
Subject: Year 2000 Member Risk Policies

Attached are draft MEC and Board materials that propose temporary changes to the Global Member Risk Policy to accommodate the Year 2000 situation. Your representatives on the Year 2000 Business Council have endorsed these changes. **If we don't hear otherwise from you by January 8th, we will send these out to the Executive Committee for early adoption, as per the discussion at the last Board meeting.**
Thanks for your consideration.

Sorry....here's the file

Y2K Board Proposal 1298

Katz, Bennett

From: Gregory, Laura
Sent: Tuesday, December 22, 1998 9:44 AM
To: Eitingon, Daniel; Katz, Bennett
Cc: Elliott, Linda; Nall, Sandy; Jaschob, Wolfgang; Held, Dick; King, Robert
Subject: Board Proposal

Linda Elliott has asked me to provide you with the Year 2000 MEC and Board materials on Member Risk (she is out of the office due to a death in the family).

The attached advance material proposes temporary changes to the Global Member Risk Policy to accommodate the Year 2000 situation. It has been developed by Wolfgang Jaschob, Dick Held, and me, and it has been reviewed and endorsed by the Year 2000 Business Council.

9901 MEC Member Risk v 4.0.doc

We believe that this will be the only topic that will require Board action. Two other Executive Summaries are planned: the standard status report, which will include performance against December milestones, and a summary of Card Acceptance topics (with no action required).

Please let Linda or me know if you have any questions or comments.

Laura Gregory
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VISA INTERNATIONAL

MANAGEMENT EXECUTIVE COMMITTEE

San Francisco, California
18-19 January 1999

EXECUTIVE SUMMARY

Year 2000 Member Risk Management

The transition to Year 2000 presents a significant challenge for financial institutions. Many automated applications could cease to function normally as a result of conventions for date fields adopted in previous decades. Failure to address this issue in a timely manner could cause banking institutions to experience settlement or operational difficulties. As a result, Visa must take the necessary steps to identify potential problems and minimize disruptions in the Visa Payment System.

Modifications to the Global Member Risk Policy and a procedure for Principal Member Year 2000 risk management will be presented for the Committee's consideration.

Background

The Visa International By-Laws (Section 2.17, 2.18, and 7.17) and the Visa International Operating Regulations, (Volume 1, Section 2.5.F, Corporate Risk Reduction Procedures), define the procedures by which Visa may terminate membership and take other actions to reduce the risks to the system. These sections are provided in Attachments A and B.

All Visa Regions are undertaking Year 2000 readiness assessments of the critical participants in the Visa payment system to determine settlement and operational (brand) risk. The results of these assessments will be provided to the Management Executive Committee and the Visa International Board of Directors. If a Principal Member is deemed to present undue risk to the Visa payment system, risk mitigating actions will need to be implemented to ensure overall safe and sound system operations. The risks Visa is exposed to principally consist of two categories:

- Settlement risk
- Operational (brand) risk

Settlement Risk

Settlement risk (a Member's ability to dis[illegible] [illegible]tions) can be mitigated by requiring Members to pledge collateral. Visa International has adopted a policy ("Global Member Risk Policy") which defines acceptable credit risk thresholds. The policy was approved by the International Board in June 1992 and subsequently revised as required. Members that are deemed to have excessive settlement risk are required to mitigate this risk through the pledging of collateral.

In preparation for the Year 2000, it is recommended that the policy be amended temporarily to reflect the uncertainties associated with settlement during this period. In light of this concern, it is proposed that the amount of collateral (where required) be increased by 50 percent unless a Region develops an internal formula to calculate settlement exposure that justifies a different requirement and that is endorsed by the International Member Risk group.

For purposes of requiring additional collateral, the Year 2000 transitional period will begin in June 1999. It is recommended that the Board delegate authority to the Management Executive Committee to determine when the transitional period for requiring the additional collateral should end. The proposed amendment to the Global Member Risk Policy is described in Attachment C. This amendment has been reviewed and endorsed by the Regional Member Risk Managers and the Year 2000 Business Council.

Operational (Brand) Risk

Operational risk is associated with a Member's ability to perform its daily activities, including its Visa activity. If a Member experiences any disruptions in their operations, Visa's reputation (brand risk) could be negatively impacted. Operational disruptions can also lead to increased fraud exposure as authorization processing is impaired or detection/screening systems are rendered inoperable. These risks are not covered under the Global Member Risk Policy, and are being assessed through Visa's Year 2000 readiness assessment undertaking. A procedure has been defined in which each Region will evaluate and mitigate the risks posed by the failure of its Principal Members to prepare adequately for the Year 2000. This procedure is described in Attachment D; it has been reviewed and endorsed by the Year 2000 Business Council.

If Members are deemed to have excessive operational risk, necessary actions to mitigate these risks will be implemented. Such actions may include working with affected Members to transfer portfolios to alternate Members/processors, suspending their Visa activity, pledging additional collateral to cover fraud exposure, as described in Attachment E, or ultimately terminating their membership.

The By-Laws provide the authority to take the actions contemplated in this procedure. Visa may need to act more frequently during the Year 2000 period than in the past and may need to have the ability to react more quickly to address material risks. Decisions on Member suspension/termination and other significant enforcement actions would generally be taken by the Management Executive Committee or the Risk Management Committee, and all actions will be reported to the Board.

Travelers Cheques

Travelers Cheque Issuers will also be reviewed for Year 2000 preparedness. However, collateral requirements will remain unchanged from the present policy requirements.

Issuers rated investment grade found to be so deficient in their Year 2000 preparedness that their ability to discharge their financial obligations in a timely manner is impaired, will be required to pledge collateral. In such cases, 100 percent of Travelers Cheque outstandings need to be collateralized.

Additionally, all Issuers will be reviewed for operational preparedness, and appropriate actions will be taken to mitigate potential risks in a timely manner. Findings will be reported to the Management Executive Committee and the Board.

Requested Action

The Management Executive Committee is requested to approve these actions in preparation for their presentation to the February meeting of the Executive Committee of the International Board of Directors.

Wolfgang Jaschob and Laura Gregory

ATTACHMENT A

VISA INTERNATIONAL BY-LAWS

Section 2.17 Involuntary Termination of Membership and Conditions of Continuing Membership

(a) For good cause only, a member may be expelled from the corporation by an affirmative vote of three-fourths (3/4) of the directors present at any meeting of the Board at which a quorum is present. Good cause shall include, by way of example but not by way of limiting the discretion vested in the Board of Directors:

(i) Repeated or willful violation of the provisions of the Certificate of Incorporation, these By-Laws, the Visa International Operating Regulations, or conditions of membership imposed by the Board of Directors;

(ii) Any act, event, or condition which reasonably leads the Board of Directors to believe that a member is or is about to become insolvent or unable to meet its obligations or requirements under the Certificate of Incorporation, these By-Laws, or the Visa International Operating Regulations (whether or not such inability is caused by the requirements of applicable law), or is operating in an unsound and unsafe manner;

(iii) Willful failure to pay at the time or in the manner specified in these By-Laws or the Visa International Operating Regulations any fees, charges, or other obligations owed by a member to the corporation; or

(iv) Refusal on the part of any member to comply with the provisions of these By-Laws or the Visa International Operating Regulations to maintain and make available to the corporation such records as will permit an accurate determination and verification of the matter contained in the certificate of sales volume.

(b) Upon voting to expel any member from the corporation, the Board of Directors shall promptly give written notice thereof to the expelled member setting forth the date on which the expelled member's membership shall terminate and the reason(s) for such termination.

(c) The Board of Directors by a three-fourths (3/4) vote of the directors present at any meeting of the Board at which a quorum is present or, in the event time does not permit a meeting of the Board or an action without a meeting without exposing the system to serious losses, the President, Executive Vice President, or any two Senior Vice Presidents of the corporation may impose conditions on any member if, in their respective opinion(s), a member's Card and/or Cheque Program (i) is not being operated in a sound and safe manner or (ii) exposes the corporation or its members to financial loss.

Section 2.18 Automatic Termination of Membership; Program Participation Eligibility

(a) Membership of a member shall automatically terminate if any one or more of the following events occurs:

(i) A bankruptcy or insolvency proceeding or its equivalent is filed by or against any such member under any applicable law(s), or a receiver is appointed to protect the assets of such member for the benefit of its creditors.

(ii) A Merchant Bank fails to convert its membership in accordance with Section 2.07(c) ("Merchant Bank Membership").

(iii) The member, after notice from the Board of Directors of the corporation, continues to act, or fails to act, in a manner that jeopardizes the corporation's rights in and to either or both of the marks, VISA and the Blue, White and Gold Bands Design, or other marks adopted by the corporation from time to time.

(iv) A member is an owner or a member of an organization described in Section 2.01(b) or 2.01(f) that is accepted into membership, except that (i) a Charter member terminated hereby shall not lose its Charter membership rights granted pursuant to Section 2.13 ("Charter Membership"), (ii) a member that becomes an owner or member of a Group Member solely for the purpose of exercising voting rights in the Group Member granted for service fees paid pursuant to Section 2.10(b) and Section 2.10(c), and (iii) a member or owner of a Group Member that acquires membership in the corporation pursuant to Section 2.22(c) shall not have its membership automatically terminated hereunder.

(b) A sponsored member's eligibility to participate in a Program shall terminate if such member, with respect to such Program, is no longer sponsored.

Section 7.17 Powers and Duties

In addition to the powers and obligations of the Board of Directors and Officers of the corporation, the Management Executive Committee shall (i) develop, approve, and recommend to the Board of Directors a strategic long-range plan and a yearly business plan, including the annual budget; (ii) regularly review performance of all regions; (iii) have the authority to approve an expenditure of up to US $5 million, provided it was contained in the approved annual budget; (iv) have the authority to approve an expenditure of up to US $2.5 million if it was not contained in the annual budget but is within the remaining contingency in the approved annual budget; (v) impose conditions of membership on a Member if, in the Committee's opinion, a Member's card or cheque program is not being operated in a sound and safe manner or exposes the corporation or its Members to financial loss; (vi) adopt or amend the Visa International Operating Regulations, provided the principles thereof have been previously approved by the Board of Directors, or a Committee thereof, by a three-fourths (3/4) vote of the directors present or, in the case of a Committee, the members present, at any meeting of the Board or such Committee at which a quorum is present; (vii) wherever the By-Laws specify that the corporation shall have certain power, as distinct from the Board of Directors, have the power to exercise those powers; (viii) oversee any and all committees of the management, such as the International Credit Risk and Investment Committee and the Employee Benefits Board; (ix) have the authority to appoint and remove officers of the corporation below the level of Executive Vice President and delegate to the Regional Presidents and the President of Products and Systems authority to appoint and remove officers of the corporation below the Executive Vice President level; and (x) any other powers the Board of Directors delegates to the Management Executive Committee by a three-fourths (3/4) vote of the directors present at any meeting of the Board at which a quorum is present or powers of the President delegated by the President to the Management Executive Committee in writing.

ATTACHMENT B

VISA INTERNATIONAL OPERATING REGULATIONS

VOLUME 1 - GENERAL RULES

2.5.F Corporate Risk Reduction Procedures

2.5.F.1 Member and Agent Responsibilities

2.5.F.1.a Upon receipt of instructions imposing conditions, as specified in Section 2.17 of the Visa International By-Laws and Regional Board Delegations, a Member or agent must implement risk reduction measures that may include, but are not limited to, the following:

- Prohibiting or limiting any of the following actions:
  - Issuing new or reissued Cards
  - Signing or re-signing Merchants
  - Using any independent sales organizations
- Blocking the Authorization of Cardholder Transactions or prohibiting Acquirers from obtaining Authorization on Transactions on behalf of certain Merchants
- Terminating some or all Merchants that either:
  - Conduct Transactions where the Cardholder is not present or where goods or services are to be delivered after the Transaction Date
  - Receive a volume of Chargebacks that substantially exceeds the system average
- Pledging collateral to secure a Member's or agent's obligations and reimbursement to Visa for any expenses incurred ensuring compliance
- Redirecting Settlement funds to avoid potential losses, as specified in Section 6.3.B.2, including, but not limited to:
  - Rerouting Settlement funds around the financial institution that normally holds the Member's or agent's funds
  - Holding funds to ensure the correct application of Cardholder funds

- Holding funds for the payment of Merchants
- Holding funds for the future payment of Chargebacks
- Withholding funds for the purpose of obtaining collateral or meeting other Member obligations
- Prohibiting or limiting a Member's right to sponsor Participant Members

- Requiring a Member to change one or more of its designated agents

2.5.F.1.b The right of Visa to limit or terminate a Member's agreement with a Merchant or an agent must be acknowledged in each Merchant and agent agreement.

2.5.F.2 Visa Rights

2.5.F.2.a Visa may implement any provision in Section 2.5.F.1 to protect the Visa payment system.

2.5.F.2.b Visa is not obligated to take actions to protect any Member, Merchant, or Cardholder from financial injury.

ATTACHMENT C

TEMPORARY AMENDMENT TO THE GLOBAL MEMBER RISK POLICY (RE: YEAR 2000) DEFINITION OF COLLATERAL SUFFICIENCY - 700.8

The required amount of collateral will be determined by the underlying cause of the collateral condition. If the cause is a below-standard Institutional Risk rating (irrespective of the Country Risk rating), then the collateral requirement will be as follows:

A. Short-Term Settlement Exposure - collateral requirement for programs in Section 500.1.

(i) Institutional Risk

New Program - Baseline Exposure:

Card Issuer - Two (2) weeks of projected third-year sales volume if reasonably ascertainable or, if not, a minimum of $50,000 to be subsequently adjusted to the degree that the collateral becomes less than 2/52nds of annualized volume.

Merchant Acquirer - One (1) week of projected first-year merchant volume.

Existing Program - Baseline Exposure:

Card Issuer - Two (2) weeks of normal sales volume as reported on the most recent Operating Certificate.

Merchant Acquirer - One (1) week of normal merchant volume as reported on the most recent Operating Certificate or six (6) months of normal chargeback volume.

Year 2000 Transitional Period -- The collateral requirement during the Year 2000 transitional period (as defined by the Management Executive Committee) will equal the Card Issuer and Merchant Acquirer baseline exposure times 1.5, unless a Region develops an internal formula to calculate settlement exposure that justifies a different requirement and that is approved by International Member Risk (IMR).

(ii) Country Risk

If the cause of the collateral condition is a below-standard Country Risk rating (and the Member's Institutional Risk rating is above-standard), then the collateral requirement will be as follows:

New Program:

Card Issuer - Two (2) weeks of projected third-year international incoming interchange if reasonably ascertainable or, if not, a minimum of $50,000 to be subsequently adjusted to the degree that the collateral becomes less than 2/52nds of annualized volume.

Merchant Acquirer - One (1) week of projected first-year merchant volume

Existing Program

Card Issuer - Two (2) weeks of normal international incoming interchange.

Merchant Acquirer - One (1) week of normal international outgoing interchange or six (6) months of normal international chargeback volume.

Notwithstanding the above, under certain circumstances additional conditions may be imposed if the cause of the collateral condition is a below-standard Country Risk rating (and the Member's Institutional Risk rating is above-standard). These circumstances include the following:

(i) If the Country Risk rating is "D" (refer to Section 600.2), the International Risk Management Committee ("IRMC") can require Members within that country to sign a "Hold Harmless Agreement", under which these Members discharge Visa of any liability if Visa settlement is not completed as a result of a domestic payment system interruption. Generally, such conditions will be applied when the domestic volume is both large and a very substantial proportion of total volume (i.e.; 85% or more). Such hold harmless agreements can only be put in place with the express approval of the IRMC.

(ii) If the Country Risk rating is "E" (refer to Section 600.2), the definition of collateral sufficiency shown above under Section 700.8.A(i) will be applied, regardless of Institutional Risk rating.

B. Long-Term Settlement Exposure - collateral requirement for programs in Section 500.2.

(i) Issuers with a below-standard rating will be required to collateralize their programs to the extent of a minimum of eighty (80) percent of total outstandings (as of quarter-end) or, if outstandings are growing very rapidly, an amount that adequately reflects the rapid rate of growth. (The minimum initial collateral requirement will be the greater of: eighty percent of total outstandings or $50,000.)

(ii) At least one-third (33.3 percent) of the collateral must be in the form of cash. Consideration will be given to taking the remainder in the form of cash-like assets or a third-party guaranty, in accordance with the terms defined in Section 700.1.

(iii) In cases in which the collateral requirement is triggered by a below-standard Country Risk rating and the country risk is deemed to be principally a short-term exposure associated with foreign exchange controls, as determined by the International Risk Management Committee (and the Institutional Risk rating is above-standard), the collateral requirement will be one-third to one-half of outstandings.[1] [TC Issuers only - the precise amount will be established by the International Risk Management Committee, taking into account the circumstances at hand, including the strategic value of the program and the expected rate of presentations.]

C. These guidelines are based on estimates of the liabilities that would ensue in a typical Member failure situation. However, to determine collateral sufficiency in any particular situation, the individual characteristics of the Member's program must be considered. For example, collateral in excess of the baseline would be appropriate with respect to a card program if the average number of days from transaction to settlement is greater than the baseline or if the Member's cardholders conduct most of their transactions in places in which a high percentage of the transactions are not authorized. Likewise, collateral below the baseline would be appropriate in cases where transactions are online (both authorization and settlement occur concurrently).

D. Members whose programs are growing very rapidly may be required to post collateral in excess of the baseline requirement defined above.

E. For purposes of establishing collateral requirements, netting of merchant or outgoing volume against sales or incoming volume, respectively, is generally not permitted. However, for countries with a rating of "C" or "D", the International Member Risk Committee may permit some degree of offset, based on a compelling case made by the Region requesting the exception.

[1] Both conditions must be met for this treatment to apply. It is expected that such treatment would be the exception rather than norm, when country risk is the cause of the collateral requirement.

ATTACHMENT D

PRINCIPAL MEMBER YEAR 2000 RISK MANAGEMENT PROCEDURE

The following procedure describes the actions to be taken in specified timeframes to evaluate and mitigate the risks posed by the failure of Principal Members to prepare adequately for the Year 2000. Each Region is responsible for carrying out this procedure for each of its Principal Members. The procedure is presented graphically on the page following this description.

1. <u>On or After March 1999, Readiness Assessment</u>. Regions will undertake quarterly Year 2000 readiness assessments of the key participants in the Visa payment system, including all Principal Members. The assessments performed during the first calendar quarter of 1999 will be used to determine which Principal Members require further investigation or action.

   If the readiness assessment determines that the Member is preparing appropriately for Year 2000 and is likely to complete the preparations successfully prior to the transition, the normal Member Risk procedures will be used to determine if collateral is required.

   If the readiness assessment determines that the Member is not preparing appropriately for Year 2000, the Region will discuss the findings with the Member. If the Member agrees with the Visa assessment, the process will continue with Step 3.

2. <u>On or After April 1999, Audit</u>. If the Member disagrees with the Visa assessment, an external auditor will be engaged to evaluate the Member's Year 2000 program.

   If the external audit report indicates that the Member is preparing appropriately for Year 2000, the normal Member Risk Procedures will be used to determine if collateral is required. Visa's determination as to whether such report indicates insufficient preparedness by a Member shall be binding on that Member.

3. <u>On or After May 1999, Encourage to Transfer Portfolio</u>. If the external auditor agrees with the Visa finding, or if the Member agrees with the initial Visa finding in Step 1, the Region will meet with the Member to understand its environment in more detail and to work with the Member to transfer its portfolio (or key merchants or cardholders) to another Member or processor who has a satisfactory Year 2000 program.

   If the Member agrees, the Region will assist the Member to transfer the program (or certain components thereof) prior to the Year 2000 transition.

4. <u>On or After June 1999, Require Additional Collateral</u>. If the Member does not agree to transfer their program, a pledge of collateral to cover both settlement and fraud risks will be required, even if the Member has not otherwise been required to pledge collateral. The collateral for fraud risk is intended to compensate for potential incremental fraud exposure if an issuing Member must use stand-in processing due to Year 2000 failures or if an acquiring Member is unable to process authorization requests. The amount of additional collateral will be calculated as described in Attachment E.

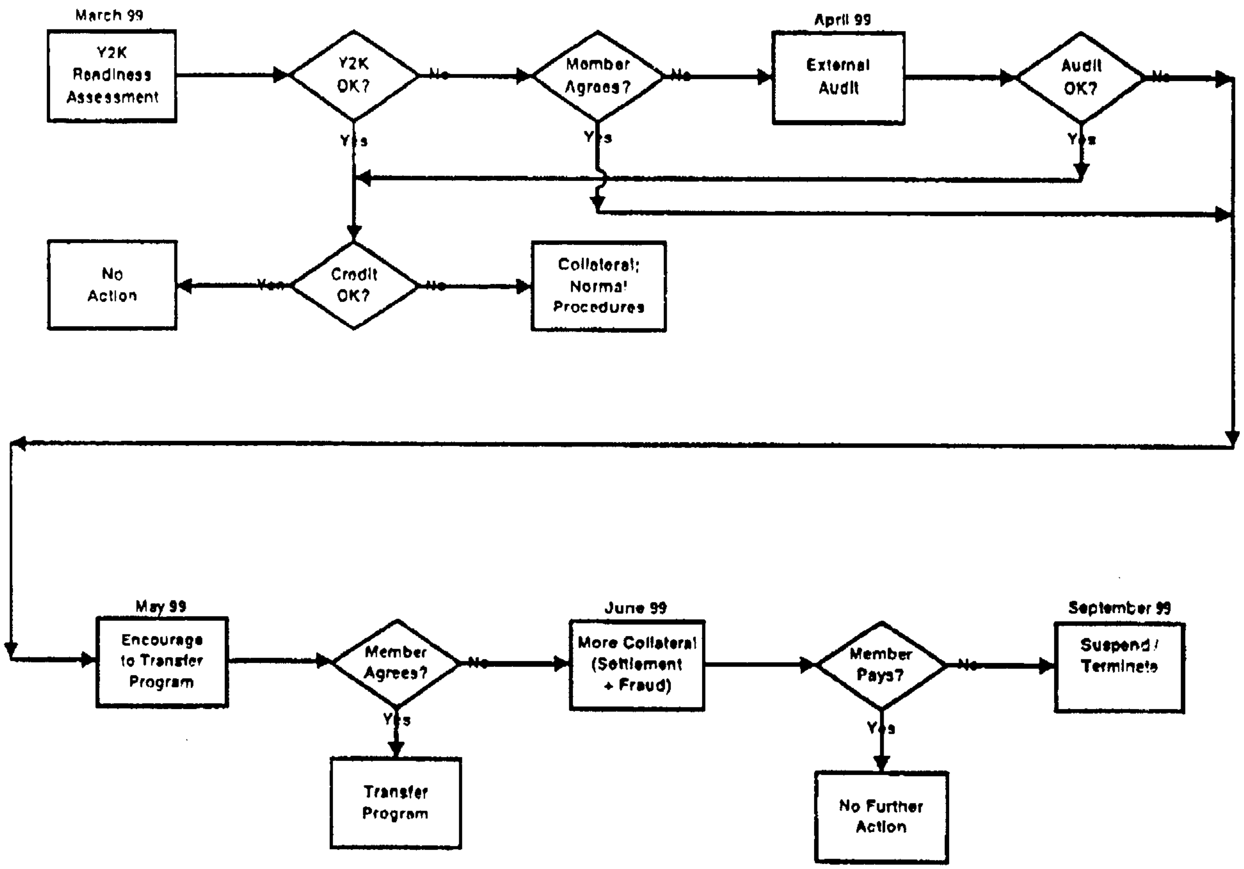
   If the Member pledges the collateral, no further action is required.

5. <u>On or After September 1999, Suspend/Terminate Member</u>. If the Member fails to pledge the required collateral, its membership will be suspended or terminated because of the material breach of the Visa International By-Laws and Operating Regulations.

   The suspension/termination process may take several forms, from an abrupt termination to a gradual wind-down of activities. Care should be taken to protect the goodwill of the Visa program during this process. If time permits, progressive actions should be undertaken to minimize the impact to the Visa brand. Such actions could include:

   - Ensure sufficient collateral is available (e.g., cover both international and national net settlement positions, lengthen pipeline, cover fraud risk).
   - Decline any transactions that do not pass CVV checking.
   - Prevent high-risk transactions (e.g., domestic ATM and branch cash advances, international cash advances, quasi-cash, mail/telephone order transactions).
   - Block all VisaNet authorizations.
   - List all BINs on the Card Recovery Bulletin.

PRINCIPAL MEMBER YEAR 2000 RISK MANAGEMENT PROCEDURE
(Settlement and Operational Risk)



ATTACHMENT E

COLLATERAL REQUIREMENTS FOR FRAUD EXPOSURE

Under current Operating Regulations the financial liability for the majority of fraud losses rests with the Issuer. The Issuer has the primary motivation to manage risk for transactions governed by routine card acceptance. The Acquirer's accountability is generally restricted to ensuring that the established standards for card acceptance are met. The consequences of Year 2000 failures occurring in the transaction process can be broadly divided into two categories – the inability of the Issuer to effectively manage risk, and the incapacity of the Acquirer to satisfy card acceptance procedures.

With respect to fraud, the impact of internal Year 2000 related non-compliance on the Issuer will likely be direct and immediate. The absence of effective controls being in place will lead to an increased exposure to fraud losses. While it is not likely that an Issuer will be targeted immediately by fraudsters, the exposure to existing fraud schemes will cause some near term loss. Further, as awareness of the Issuer exposure develops, the probability of a targeted attack will increase significantly. This is particularly important in the instance of focused and organized attacks, such as the account generated fraud schemes that were identified in the third and fourth quarters of 1998.

An equally significant exposure to the Issuer will result from the Year 2000 failure of Merchants and Acquirers and the consequent fallback to inferior card acceptance practices (e.g., from magnetic stripe to key entry or paper). The fallback will deprive the Issuer of many key risk control functions, without providing a corresponding relief from exposure to fraud or credit losses.

The fraud liability of the Acquirer is largely indirect – resulting primarily from cardholder disputed transactions that are charged back by the Issuer. Additional Acquirer exposure emanates from automated chargeback reduction services that act on improperly processed transactions (below floor limit activity on accounts with pick-up status).

For these reasons, under the conditions described in the Principal Member Year 2000 Risk Management Procedure, a pledge of additional collateral to cover fraud exposure will be required. The amount of this collateral will be determined for Issuers and Acquirers as described below.

Issuer Collateral Requirements

Collateral requirements to cover fraud exposure for Issuers shall be the greater of:

1. A provision for catastrophic risk resulting from a focused attack (e.g., account generated fraud scheme), set at U.S. $1 million.

OR

2. The estimated fraud exposure based on the Member's historical performance, using the elements outlined below.

    1. 1st quarter fraud losses for 1998
    2. Rate of growth in fraud 1Q97 to 1Q98
    3. Volume of losses attributable to high risk markets (Year 2000 Red and Yellow zone countries)
    4. Ratio of pick-up responses to transactions
    5. Ratio of decline responses to transactions
    6. Sales volume

The following formula will determine the amount of collateral required:

((1Q98 Sales) times (1998 fraud to sales ratio) times (Rate of sales growth for running 4 quarters ending 3Q98))

+ (Volume of 1Q98 fraud losses in Year 2000 Red and Yellow countries)

+ (1Q98 Sales) times (Ratio of pick-up to Sales)

+ (1Q98 Sales) times (Ratio of declines to Sales) times (50%)

Rationale:

- Issuer fraud liability will be similar to comparable periods in prior years, adjusted for growth in volume.
- Issuer liability in high-risk countries for Year 2000 failure will increase as a direct consequence of the premeditated attacks attracted by anticipated fallback card acceptance procedures in those markets.

- Issuer exposure to fraud will be compounded by the inability to apply account status information to incoming authorization requests.
- Note: due to the lack of credit loss information it is not possible to estimate the impact of runaway credit losses and related cardholder fraud. It is likely, however, that these exposures will be substantially higher than normal.

Acquirer Collateral Requirements

Collateral requirements to cover fraud exposure for Acquirers shall be based on the following elements:

1. 1st quarter Acquired fraud for 1998
2. Rate of growth in Acquired fraud 1Q97 to 1Q98
3. Authorization rates by POS entry mode (90,02,01) for Acquirer (default to market if necessary)
4. Chargeback to sales ratio for running four quarters ending 3Q98

The following formula will determine the amount of collateral required:

(1Q98 Sales) times (Ratio of chargeback to sales for running four quarters ending 3Q98)

+ ((1Q98 Sales) times (1998 fraud to sales ratio) times (Rate of sales growth for running four quarters ending 3Q98))

+ (1Q98 Sales) times (Ratio of POS 90/Sales) times (Decline/sales ratio) times (80%)

+ (1Q98 Sales) times (Ratio of POS 02/Sales) times (Decline/sales ratio) times (50%)

+ (1Q98 Sales) times (Ratio of POS 01/Sales) times (Decline/sales ratio) times (80%)

Rationale:

- Acquirer exposure to chargeback liability will be similar to current chargeback rates for above floor transactions.

- Acquirer exposure to fraud liability will be similar to what would have occurred in comparable periods in prior years if compliance with card acceptance standards had not been met.
- Acquirer liability will increase as a consequence of reverting to sub-standard card acceptance practices due to terminal malfunction or other infrastructure failure.
- The exposure due to fallback card acceptance practices will be most extreme in circumstances where Issuers are currently disposed to decline transactions based on fraud attributes (POS 90 CVV mismatch, POS 01 with expiration date errors, etc.).
- The exposure due to fallback card acceptance practices will be least significant in circumstances where Issuers are currently disposed to decline transactions based on general fraud avoidance (POS 02 with limited transaction detail).

NOTES TO THE AGENDA

Year 2000 Member Risk Management. The transition to Year 2000 presents a significant challenge for financial institutions. Many automated applications could cease to function normally as a result of conventions for date fields adopted in previous decades. Failure to address this issue in a timely manner could cause banking institutions to experience settlement or operational difficulties. As a result, Visa must take the necessary steps to identify potential problems and minimize disruptions in the Visa Payment System. Modifications to the Global Member Risk Policy and a procedure for Principal Member Year 2000 risk management will be presented for the Committee's consideration. An Executive Summary is included.

Product Development
Guidelines

McWhinney, Deborah

From: McWhinney, Deborah
Sent: Friday, January 08, 1999 3:29 PM
To: Barnes, Ray; Cobb, Anne; Eitingon, Daniel; Fry, Derek; Goggin, Dennis M.; Katz, Bennett; Partridge, James; Pascarella, Carl; Van Der Velde, Hans; Williamson, Malcolm
Cc: Giesker, Theresa; De Wouters, Geraldine; Everoski, Dee; Spiller, Kaye; Sho, Hairei; Shields, Susie; Powell, Alicia; Ponzo, Terri; Vincent, [illegible]; [illegible], Madeleine; Burry, [illegible]
Subject: A Message From Dan Eitingon
Importance: High

DATE: JANUARY 8, 1999

TO: MEC Members

FROM: Deborah McWhinney
GSS Planning

SUBJECT: Product Development Guidelines

Pursuant to the last MEC Meeting, attached are the Region vs. Central Roles and Responsibilities documents for discussion.

If you or your team have questions, please contact me 6(720)3480, or, Barbara Kelly 6(720)2742.

Attachments:

Proposal (Mec Prod Dev).doc | Diagrams 1 & 2 (Mec Prod Dev).ppt | Appendix A (Mec Prod Dev).doc | Appendix B (Mec Prod Dev).doc

 VIF0523296

Product Development Guidelines Proposal

The attached document summarizes our recommendation on how product development should proceed at Visa. The goal of this effort is to promote regional creativity and leadership in the development of new products or services, while at the same time building appropriate safeguards to prevent spill-over problems to other regions or to the center.

Basically, we are proposing that all new product/service development activities follow the process outlined on *Diagram #1*, which is already in place in several regions, and within GSS, and seems to work well.

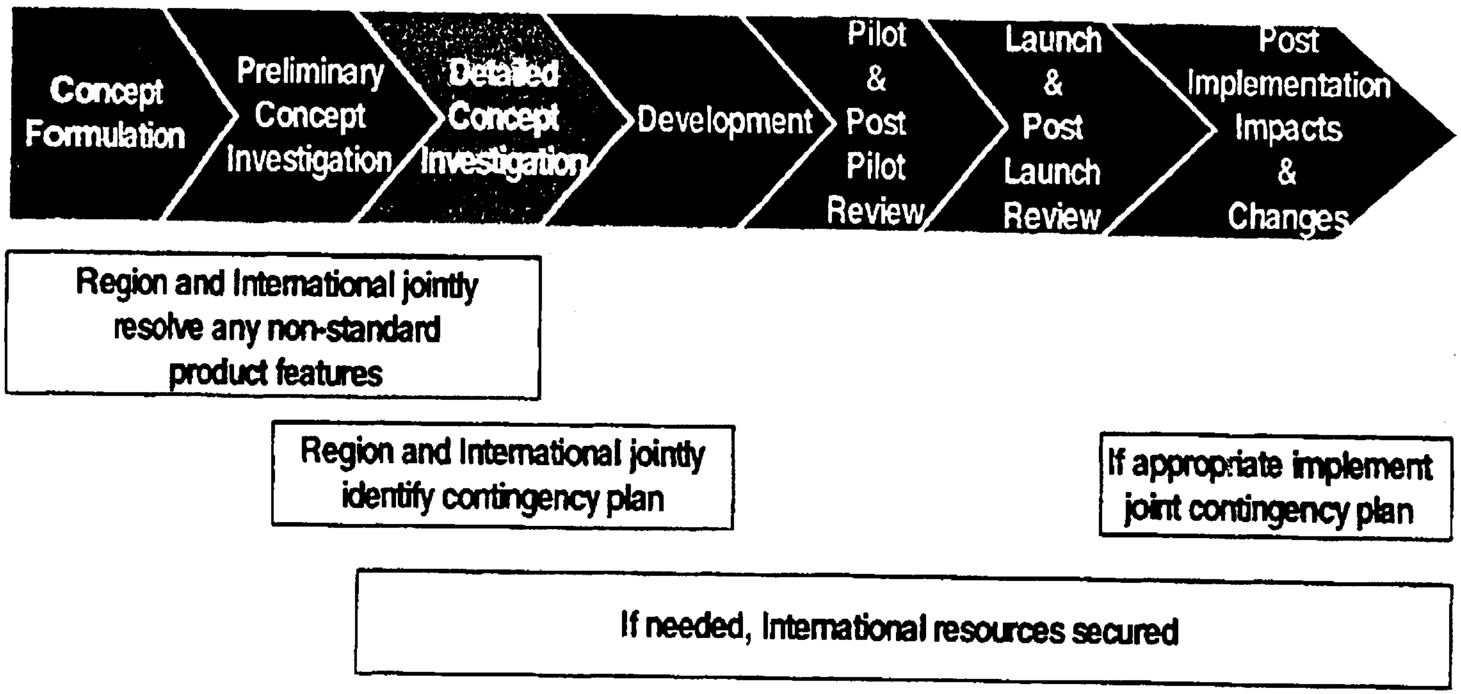
During the product definition phase, a set of Visa standards would be available from Central (*Appendix A* details a possible list, the responsible organization and their current status) to alert the developers to potential conflicts. At this time too, the originators would work with GSS to determine if the project should be funded by the requester alone or through a shared funding pool. If the product would primarily benefit the requesting region, and not be applicable globally within a short period of time, then regional funding would be appropriate. Conversely, if the product did have immediate global implications, then shared funding would be the appropriate path. *Diagram #2* details the overall decision flow.

If funding was regional, and all Visa standards issues could be satisfied, including how the product might be "converged" into a global product at a later date, then the next question would be whether GSS resources would be needed in the development process. If not, the region would be free to move forward on its own. If GSS resources were needed, availability of resources would first have to be determined according to the relative size of the effort. Larger efforts would be reviewed by the new Funds Allocation committee for financial impact determination.

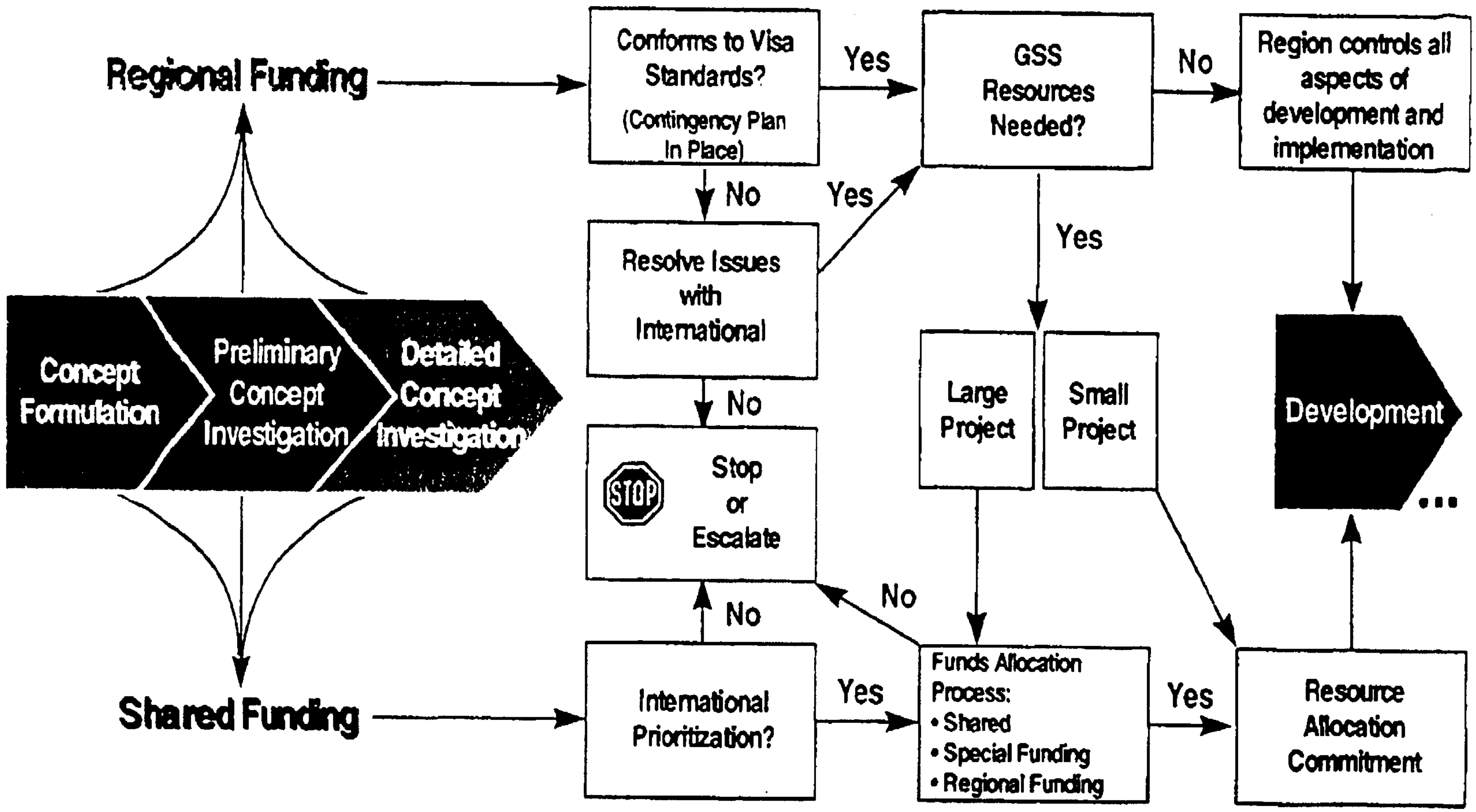
Projects that were implemented without appropriate consideration to the standards would be required to be brought into conformance, at full cost to the violating region. *Appendix B* contains sample templates for the standards approval process.

The last few pages detail how this process might work (or have worked) in several different scenarios, both real and hypothetical. The purpose of these examples is simply to demonstrate how this process would adapt to the real world.

Regional Product Development
Stages & Gates



Regional Product Development Decision Template



APPENDIX A

Visa International New Product/Service Standards

	VISA STANDARDS DOCUMENT	SPONSOR	STATUS
	BRAND		
1	Visa Flag Symbol guidelines and reproduction specifications	International Marketing	Approved
2	Visa Electron Symbol guidelines and reproduction specifications	International Marketing	Approved
3	Visa Card & Mark specifications	International Marketing	Approved
4	Visa Cash symbol	International Marketing	Approved
5	Visa ATM Signage guidelines	International Marketing	Approved
6	Visa Web Site design standards	International Marketing	Approved
7	Sydney Olympic Standards Manual	International Marketing	Approved
8	Enhanced Visa Wordmark guidelines & reproduction specifications	International Marketing	Approved
9	Visa Corporate stationary and business cards specification	International Marketing	Approved
10	Visa Presentation Standards for PowerPoint	International Marketing	Approved
11	Global Marketing Materials	International Marketing	Pending
	PRODUCT		
12	Credit Card Guidelines - Visa Op. Regs.	Current Product & Services	Approved
13	Debit Card Guidelines - Visa Op. Regs.	Current Product & Services	Approved
14	Commercial Card Guidelines	Current Product & Services	Pending
15	Card Acceptance Guidelines	Current Product & Services	Pending
16	CHIP Operating Principles	Emerging Products	Approved
17	Electronic Commerce	Emerging Products	Pending
18	Emerging Product Review Committee	Emerging Products	Approved
19	Visa Corporate Extranet Policy	Current Product & Services	Pending
	SERVICE		
20	TBD		
	DATA QUALITY		
21	TBD		
	SYSTEMS		
22	Outsourcing Guidelines 7.0	VisaNet Systems	Drafted
23	TBD		
	OPERATIONS	Processing Services	
24	TBD		
	RISK		
25	Vendor Central Approval Authority	International Risk	Approved
26	New Payment Technology	International Risk	Pending
27	Certificate Authority Providers	International Risk	Pending
28	PIN Entry Devices	International Risk	Pending
29	Payment Gateway	International Risk	Pending
	INFORMATION SECURITY		
30	Information Classification	Information Security	2Q99
31	Compliance Controls	Information Security	2Q99

APPENDIX B

REGIONAL NEW PRODUCT & SERVICE ASSESSMENT FORM				
REGION: **SPONSOR:**			**NEW PRODUCT/SERVICE NAME:**	
BACKGROUND:				
STANDARDS MET	YES	NO	AUTHORIZED BY REGION	INTERNATIONAL
1. BRAND				
2. PRODUCT				
3. SERVICE				
4. SYSTEMS				
5. DATA INTEGRITY				
6. OPERATIONS				
7. RISK				
8. INFORMATION SECURITY				
CONTINGENCY PLAN ASSESSMENT	YES	NO	REGION	INTERNATIONAL
1. Pilot Extension Plan				
2. Pilot Rollout Plan				
3. Globalization Plan				
4. Exit Plan				
DESCRIBE EXCEPTION/VARIANCE TO STANDARDS NOTED ABOVE: **RESOLUTION:**				
REGIONAL REVIEW SIGNATURE:			**INTERNATIONAL REVIEW SIGNATURE:**	

APPENDIX B

Regional New Product & Service Assessment Form

(EXAMPLE #1 - International Standards NOT Met - Real Scenario)

REGION: EUROPEAN UNION SPONSOR: JON PRIDEAUX, EVP	NEW PRODUCT/SERVICE NAME: BARCLAYS - VISA CASH GSM* LOAD

BACKGROUND:

Barclays Bank has been working with the EU region to develop a Visa Cash card that can be loaded via a cell phone. A cell phone is being modified to accept a Visa Cash card with PIN access. However, the PIN access is not Visa standard. When the cell phone specification was developed for access through Visa, the firewall protection was not in place. Visa supports the new product concept, however Visa standards for this product need to be developed.

*GSM-Global Specification for Mobile phones.

STANDARDS MET	YES	NO	AUTHORIZED BY REGION	INTERNATIONAL
1. BRAND	X		(Name of Person Here)	(Name of Person Here)
2. PRODUCT	X		"	"
3. SERVICE	N/A		"	"
4. SYSTEMS	X		"	"
5. DATA INTEGRITY	X		"	"
6. OPERATIONS		X	"	"
7. RISK		X	"	"
8. INFORMATION SECURITY		X	"	"
CONTINGENCY PLAN ASSESSMENT	**YES**	**NO**	**REGION**	**INTERNATIONAL**
1. Pilot Extension Plan	X		(Name of Person Here)	(Name of Person Here)
2. Pilot Rollout Plan	X		"	"
3. Globalization Plan		X	"	"
4. Exit Plan	X		"	"

DESCRIBE EXCEPTION/VARIANCE TO STANDARDS NOTED ABOVE:

This is a new product idea for Visa. Operations standards are not in place today for this product. The Risk and Information Security standards are not in compliance. The Cell Phone is not a secure device for PIN entry. The PIN entry that will be used does not comply with Visa Security requirements. The fire wall protection for Visa is not in place at this time.

Globalization - This product is unique for Barclays Bank and the UK, as well as for Visa. This will be a learning experience for Visa and it is not necessarily transferable at this time.

RESOLUTION:

The Risk and Information Security exception - Robyn Strang from Information Security will grant a waiver on condition that the region commit to a detailed plan for compliance with Visa's Risk and Security standards by 3QTRFY99. The EU region is being asked to accept all liability for this new product should it be compromised before it meets all Visa Standards.

REGIONAL REVIEW SIGNATURE:	INTERNATIONAL REVIEW SIGNATURE:

APPENDIX B

REGIONAL NEW PRODUCT & SERVICE ASSESSMENT FORM				
(EXAMPLE #2 - International Standards NOT Met - Real Scenario)				
REGION: US **SPONSOR:** BRUNO PERRAULT, VP			**NEW PRODUCT/SERVICE NAME:** VISA FLEET SERVICE	
BACKGROUND: The fleet service was developed on behalf of the USA region, to support the need to provide a competitive service in order to meet the requirements laid out by the GSA. In order to be authorized to compete for agency business, fleet fuel and maintenance payment service was required.				
STANDARDS MET	YES	NO	**AUTHORIZED BY** **REGION**	**INTERNATIONAL**
1. BRAND	X		(Name of Person Here)	(Name of Person Here)
2. PRODUCT	X		"	"
3. SERVICE	X		"	"
4. SYSTEMS	X		"	"
5. DATA INTEGRITY	X		"	"
6. OPERATIONS	X		"	"
7. RISK		X	"	"
8. INFORMATION SECURITY		X	"	"
CONTINGENCY PLAN ASSESSMENT	YES	NO	**REGION**	**INTERNATIONAL**
1. Pilot Extension Plan	X		(Name of Person Here)	(Name of Person Here)
2. Pilot Rollout Plan	X		"	"
3. Globalization Plan	X		"	"
4. Exit Plan	X		"	"
DESCRIBE EXCEPTION/VARIANCE TO STANDARDS NOTED ABOVE: **RISK/INFORMATION SECURITY:** Vehicle Cards - One of the significant departures from standard card processing with fleet, is the industry practice of assigning card accounts to a vehicle rather than a cardholder. While on the face of it, this is not difficult, there are implications relating to merchant procedures, cardholder verification and compliance rights. **RESOLUTION:** A review was undertaken by Visa USA Operating Regulation staff, and operating principles relating to Vehicle Cards were developed and ultimately approved by the Visa USA Board of Directors. It was the opinion of Visa USA Operating Regulation staff that there was no impact to Visa International Operating Regulations, and thus the principles were not formally reviewed with GSS Op Reg staff. When Visa Canada sought to adopt similar principles, it was pointed out that these principles were in contradiction to Visa International Operating Regulations (with respect to chargeback and compliance rights). At this point, rather than requesting a variance for Visa Canada and Visa USA, it was decided to pursue adoption of vehicle card Operating Principles at the Visa International level. Trying to look a bit down the road, the principles were written to cover not only Visa Purchasing (the scope of USA and Canada regulations), but also Visa Business and Visa Corporate - as interest had been expressed in extending this service to the other products				
REGIONAL REVIEW SIGNATURE:			INTERNATIONAL REVIEW SIGNATURE:	

APPENDIX B

REGIONAL NEW PRODUCT & SERVICE ASSESSMENT FORM				
(EXAMPLE #3 - International Standards NOT Met - Real Scenario)				
REGION: INTERNATIONAL MARKETING SPONSOR: JAN SODERSTROM			NEW PRODUCT/SERVICE NAME: INTERNATIONAL MARKETING EXTRANET FACILITY	
BACKGROUND: The International Marketing Group wants to establish an extranet facility with vendor and agency business partners to facilitate sharing of marketing programs, interactive communications and design and sign-off process. Contracted external vendors will design and create a web site service for Visa.				
STANDARDS MET	YES	NO	AUTHORIZED BY REGION	INTERNATIONAL
1. BRAND	X		(Name of Person Here)	(Name of Person Here)
2. PRODUCT		X	"	"
3. SERVICE	X		"	"
4. SYSTEM	X		"	"
5. DATA INTEGRITY	X		"	"
6. OPERATIONS	X		"	"
7. RISK		X	"	"
8. INFORMATION SECURITY		X	"	"
CONTINGENCY PLAN ASSESSMENT	YES	NO	REGION	INTERNATIONAL
1. Pilot Extension Plan	X		(Name of Person Here)	(Name of Person Here)
2. Pilot Rollout Plan	X		"	"
3. Globalization Plan	X		"	"
4. Exit Plan	X		"	"
DESCRIBE EXCEPTION/VARIANCE TO STANDARDS MARKED ABOVE: PRODUCT STANDARD EXCEPTION: External vendors were contracted to design and create an external web service. This web service is an exception to the "proposed" service standards for the Visa Corporate Extranet. The proposed service violates Visa risk and information security standards for communications inside the Visa firewall. RESOLUTION: This situation was resolved by using the Visa On-Line Business Office within GSS by creating applications using the Visa On-Line platform for secure communications and data delivery.				
REGIONAL REVIEW SIGNATURE:			INTERNATIONAL REVIEW SIGNATURE:	

APPENDIX B

REGIONAL NEW PRODUCT/SERVICE ASSESSMENT FORM	
(EXAMPLE #1 - International Standards Met - Hypothetical Scenario)	
REGION: REGION Y **SPONSOR:** JOHN JONES	**NEW PRODUCT/SERVICE NAME:** STANDALONE DOMESTIC EFTPOS SYSTEM

BACKGROUND: Hypothetical scenario: Country X has a need for a domestic EFTPOS system and mark with 100% PIN, SMS and 19-digit support. International debit acceptance is not required. Members in Country X have approached Region Y for both a technical solution and an acceptance mark. Region Y has complied with the Brand standards choosing ZORK, without links to the Visa Brand, so there would be no confusion with international Visa acceptance locations. Region Y will locally build a switch to operate the domestic system which requires no interfaces to the VisaNet systems. Funding will be shared by Region Y and participating Members.

STANDARDS MET	YES	NO	AUTHORIZED BY REGION	AUTHORIZED BY INTERNATIONAL
1. BRAND	X		(Name of Person Here)	(Name of Person Here)
2. PRODUCT	X		"	"
3. SERVICE	X		"	"
4. SYSTEMS	X		"	"
5. DATA INTEGRITY	X		"	"
6. OPERATIONS	X		"	"
7. RISK	X		"	"
8. INFORMATION SECURITY	X		"	"
CONTINGENCY PLAN ASSESSMENT	**YES**	**NO**	**REGION**	**INTERNATIONAL**
1. Pilot Extension Plan	X		(Name of Person Here)	(Name of Person Here)
2. Pilot Rollout Plan	X		"	"
3. Globalization Plan	X		"	"
4. Exit Plan	X		"	"

DESCRIBE EXCEPTION/VARIANCE TO STANDARDS MARKED ABOVE:
In this scenario, all standards have been met. Since the VisaNet system or Visa brand is not involved, the endeavor is completely self-contained within Region Y. With no role for the Visa brand or VisaNet solution, one might question why is Visa involved at all. Members in Country X value Region Y's experience and see this as an opportunity to improve the profitability of their domestic debit program. Since Visa's charter is to improve Member profitability and Region Y sees this as a terrific opportunity to control domestic processing; the endeavor is fully endorsed by Region Y's Board.

RESOLUTION:
Even though all the above standards have been met, it is proposed that the following product and systems standards be created to enable this endeavor to ultimately further the Visa brand, the Visa global acceptance infrastructure and interoperability:

- A commitment to use VisaNet message format and processing standards to facilitate interoperability for future cross border transactions.
- Visa card numbering structure to facilitate global interoperability.
- POS and ATM devices supporting the acceptance of Visa's mag. stripe and chip standards.
- Use of Visa Flag or Visa Electron for future global acceptance. Consideration of using Visa Electron as a domestic only mark in the interim.

REGIONAL REVIEW SIGNATURE:	INTERNATIONAL REVIEW SIGNATURE:

Discussion on Executive Remuneration

A.O.B. and Roundup

Miscellaneous